Be Careful What You Ask For: When Do You Want an Examiner, Receiver, CRO, Trustee, or other Neutral?

I. Overview and Introduction.

A. This section of the seminar will address the issue of neutrals. What is a "neutral?" Probably the best example of a neutral person is a judge. Neutrals are individuals who essentially meet the ethical and legal standard one expects for judges, but who are appointed or selected in various courts by the Judge or the parties to fill various roles in the case with the goal being that the addition of the neutral person to the case will facilitate a more efficient resolution of particular issues.

B. The general standard was stated succinctly by the Supreme Court: "[A judge] should, however, in pending or prospective litigation before him be particularly careful to avoid such action as may reasonably tend to awaken the suspicion that his social or business relations or friendships, constitute an element in influencing his judicial conduct." Commonwealth Coatings Corp. v. Cont'l Cas. Co., 393 U.S. 145, 149–50, 89 S. Ct. 337, 339–40, 21 L. Ed. 2d 301 (1968).

II. Bankruptcy Trustees in Chapter 11 Cases.

A. Keith

Chapter 11 Trustees

"We've got to get someone in there that can run the company!" says your creditor client. "These guys don't know what they are doing and keep stealing all the money."

"How about if we ask the court to appoint a Chapter 11 trustee," you say. "Then someone with neutrality can run the company and report to the court. It would even result in exclusivity being lifted, and we could file our own plan if we wanted to."

[*Interlude of indeterminate length*]

"I can't believe the Chapter 11 trustee just doesn't get it. He's suing me for a preference and breach of contract. To make matters worse, he's hired the most expensive lawyer in town, and it's too expensive to file my own plan and disclosure statement because I have to pay you and the trustee's lawyers. Why did you talk me into seeking the appointment of a Chapter 11 trustee?"

Not all cases are right for the appointment of a Chapter 11 trustee as the above discussion demonstrates. There are, however, times when a trustee can break log jams and bring sanity to difficult (think impossible) cases. And, the right Chapter 11 trustee, can even be a miracle worker in the eyes of some. So before we get into the exotic, let's discuss the basics of Chapter 11 Trustees:

Code section: 11 U.S.C. 1104(a) provides that any time between the filing of the bankruptcy case and before confirmation of a plan, the court may appoint a Chapter 11 trustee for cause including fraud, dishonesty, incompetence or gross mismanagement. Finally, a trustee may be appointed in the best interests of creditors, equity security holders, or other interests of the debtor's estate.

The language of the Code provides:

(a) At any time after the commencement of the case but before confirmation of a plan, on request of a party in interest or the United States trustee, and after notice and a hearing, the court shall order the appointment of a trustee—

(1) for cause, including fraud, dishonesty, incompetence, or gross mismanagement of the affairs of the debtor by current management, either before or after the commencement of the case, or similar cause, but not including the number of holders of securities of the debtor or the amount of assets or liabilities of the debtor; or

(2) if such appointment is in the interests of creditors, any equity security holders, and other interests of the estate, without regard to the number of holders of securities of the debtor or the amount of assets or liabilities of the debtor.

While the moving party bears the burden of proof to have a trustee appointed, there is no prescribed standard, especially given the strong presumption that the debtor remain in possession postpetition. It is important to note that this is one area where the Court maintains maximum discretion and may appoint a trustee after a full evidentiary hearing or facts that are a matter of record. In fact, while most Chapter 11 trustee appointments are the result of a motion filed by the UST or other party in interest, courts have found authority to appoint trustees sua sponte.

Standard for Appointment: The default rule in Chapter 11 is that present management remains in place upon filing of the bankruptcy petition. Debtors in possession control and manage their own affairs within the confines of the Chapter 11 process including reporting and disclosure obligations as set out in the Bankruptcy Code and Federal Rules of Bankruptcy Procedure. Because a trustee appointment upsets this balance and the normality of a Chapter 11 case, it is a significant event in the life of a Chapter 11 case. Additionally, the cost, expense, and uncertainty of a Chapter 11 trustee make it something most courts issue sparingly. The evidence considered by a Court in appointing a Chapter 11 trustee generally is taken from a review of the "totality of the circumstances."

When considering whether to appoint a trustee for cause, courts may consider both the pre- and postpetition misconduct of a debtor's management, but courts should not consider predictions as to management's future conduct. The fact that a debtor's prior management might have been guilty of fraud, dishonesty, incompetence, or gross mismanagement does not necessarily provide grounds for the appointment of a trustee, as long as a court is satisfied that the current management is not similarly guilty and/or is taking sufficient steps to remedy the wrongs committed by prior management.

The most common basis for appointing a trustee is gross mismanagement and/or incompetence. In order for this appointment to be made, the debtor's management must show a willingness to depart from ordinary business judgment to a degree that it can no longer be afforded deference. The factors used to determine whether or not management is guilty of gross mismanagement may vary depending up on the facts of the case. Some factors and fact-specific analysis for the appointment of a trustee have included the need for a neutral party to mediate disputes between the debtor and its creditors, acrimony between debtor and creditor, management conflicts of interest, breaches of fiduciary duties ; excessive intercompany transfers. While there are other factors that may apply in specific circumstances, one may assert that "you know it when you see it." A good example of a case where the Court noted its power to appoint a trustee either on motion or sua sponte after consideration of a voluminous record including a debtor in possession prone to excessive litigation is In re Thomas.

Cause to appoint a trustee is not a defined term in the Bankruptcy Code. Whether a particular act or omission rises to the level of cause requires consideration of all pertinent facts and circumstances.

Unlike § 1104(a)(1) 's mandatory provision, § 1104(a)(2) "envisions a flexible standard." Section 1104(a)(2) expressly provides that the court shall order for the appointment of a trustee in a Chapter 11 case if it is in the best interests of the creditors and the estate. "The flexible standards embodied in § 1104(a) are intended to accommodate two goals: (1) facilitation of the debtor's reorganization; and (2) protection of the public interest and of creditors." 7 Collier on Bankruptcy ¶ 1104.02[3][a] (16th ed. 2016) (citing H.R. 8200, 94th Cong. § 1104 (1978)). The "interests" standard appears to be more of a balancing test; that is, whether the benefits to all interests of the estate that would come from the appointment of a chapter 11 trustee outweigh the detriment of the estate. Courts have considered various factors when utilizing this balancing test, including: "(1) the trustworthiness of the debtor; (2) the debtor's past and present performance and prospect for rehabilitation; (3) whether the business community and creditors of the estate have confidence in the debtor; and (4) whether the benefits outweigh the costs." LHC, 497 B.R. at 293 (citations omitted). It should be noted that "[a]ppointment of a trustee under § 1104(a)(2) is within the sound discretion of the bankruptcy judge." Id . (citations omitted).

Rules and notice: Federal Rule of Bankruptcy Procedures 2007.1 provides that a motion for an order to appoint a trustee or an examiner under Section 1104(a) of the Bankruptcy Code shall be made in accordance with Rule 9014. Further, a request to convene a meeting of creditors for the purpose of electing a trustee in a chapter 11 reorganization case shall be filed and transmitted to the United States trustee in accordance with Rule 5005 within the time prescribed by Section 1104(b) of the code. Pending court approval of the person elected, any person appointed by the United States trustee under Section 1104(d) and approved in accordance with the provisions of FRBP 2007.1(c).

FRBP 2009 allows the court, in the absence of conflicts, to order one trustee over jointly administered cases but leaves open the possibility of separate trustees if conflicts of interest would be created by one trustee sitting over multiple debtors.

Chapter 11 trustees should be aware of FRBP 2015, which requires the filing and transmission to the UST of a complete inventory of the property of the debtor within 30 days after qualifying as a trustee, unless the inventory has already been filed. The same rule also requires records of receipts and disposition of money and property. Furthermore, Chapter 11 trustees must be disinterested. FRBP 2014(a). Disclosure of contacts is key and the disclosure should be timely and thorough.

Who selects the Chapter 11 trustee: The U.S. Trustee, after consultation with parties in interest, appoints a disinterested person. The trustee appointment is subject to court approval. While the actual appointment of the trustee may seem like a black box, the Office of the United States Trustee has provided some guidance. The UST consults with creditors and parties in interest to find a qualified candidate. Parties are allowed to recommend candidates. The U.S. Trustees look first for independence. Then, the experience of a candidate is considered.

Payment: The Chapter 11 trustee gets paid under and is limited to the compensation described in Section 326 of the bankruptcy code and paid under Section 330 unless the court orders otherwise.

Benefits of a Chapter 11 Trustee Appointment

The primary benefit of a Chapter 11 trustee is a neutral officer to take control of the affairs of a Chapter 11 debtor. Most courts acknowledge the important role of the trustee, and in many cases actually provide deference to the appointed candidate.

Aside for acting for the debtor in possession, a strong Chapter 11 trustee has the unique opportunity to build consensus among disparate and often warring factions. Talented trustees take their appointment as a gateway to meeting with all parties affected by the bankruptcy case, assess operations, and then propose a plan or final solution.

Drawbacks of a Chapter 11 Trustee

Cost is a major drawback of a Chapter 11 trustee. Most trustees will insist upon hiring qualified professional and will require time to get up to speed.

The devil you know is sometimes better than the devil you don't. Many a creditor has moved for the appointment of a Chapter 11 trustee only to get exactly what they asked for, and like a dog chasing a car have asked the question, "now that I've caught it, what do I do with it?"

III. Bankruptcy Examiners.

A. John Young

[Examiners section follows. (30 pages)]

EXAMINERS IN BANKRUPTCY CASES

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I. GROUNDS FOR APPOINTMENT OF EXAMINER

Under section 1104(c) of the Bankruptcy Code, the court, on request of a party in interest or the United States Trustee, is instructed to order the appointment of an examiner if one of two conditions is met:

(1) the appointment is in the interests of creditors, any equity security holders, and other interests of the estate (11 U.S.C. § 1104(c)(1)); or

(2) the debtor's fixed, liquidated, unsecured debts, other than debts for goods, services, or taxes, or owing to an insider, exceed $5,000,000 (11 U.S.C. § 1104(c)(2).

The statute further provides that an examiner should not be appointed if a chapter 11 trustee has been appointed or if a plan has been confirmed.

A. Is 1104(c)(2) Really Mandatory?

The two grounds for the appointment of an examiner have given rise to some litigation, particularly over whether the mandatory examiner requirement of section 1104(c)(2) is in fact mandatory. The terms of the statute seems straight forward: if the debtor has more than $5 million in qualifying claims, the court "shall order" the appointment of an examiner if a party with standing moves for the appointment. The history behind this provision supports the mandatory nature of the appointment. During the debates leading to the adoption of the Bankruptcy Code in 1978, it appears that one of the more contested issues was whether a trustee would be mandatory for some or all chapter 11 debtors. The House bill called for discretionary trustee appointment based upon cost-benefit analysis. The Senate version, on the other hand, made trustee appointments mandatory for "public companies" with defined liabilities of more than $5 million and at least 1,000 equity security holders. The compromise that became law adopted the "presumption" that the debtor would remain in possession, but called for the mandatory appointment of an examiner if the debtor had more than $5 million in qualifying claims. *See* Leonard L. Gumport, *The Bankruptcy Examiner*, 20 Cal. Banker. J. 71, 83-97 (1992).

B. Courts are Divided on "Mandatory" Appointment

Despite the clear statutory history, parties have often argued that section 1104(c)(2) (and its predecessor section 1104(b)(2)) do not mandate the appointment of an examiner. The leading circuit court authority on this issue is *Morgenstern v. Revco D.S., Inc. (In re Revco D.S., Inc.)*, 898 F.2d 498 (3d Cir. 1990) (mandatory language is in fact mandatory). Although most courts have confirmed that the section 1104(c)(2) examiner appointment is mandatory, a few have focused on the "as is appropriate" language to hold that if an investigation is not appropriate, no examiner need be appointed. *See U.S. Bank Nat'l Ass'n v. Wilmington Trust Co. (In re Spansion, Inc.)*, 426 B.R. 114 (Bankr. D. Del 2010). Other courts have rejected this reasoning, holding that reading the statute in this manner conflates subsections (c)(l) and (c)(2) by making both dependent upon a court's determination that an investigation is appropriate. *See Walton v. In re Cornerstone Ministries Investments, Inc.*, 398 B.R. 77 (N.D. Ga. 2008) (reversing bankruptcy court); *In re UAL Corp.*, 307 B.R. 80,84 n.2 (Bankr. N.D. III. 2004) ("[I]f paragraph (c)(2) were not mandatory, then

§ 1104(c) would have the following meaning: 'If specified debt is less than $5 million, it is in the court's discretion to appoint an examiner; and if specified debt is more than $5 million, it is in the court's discretion to appoint an examiner.'"). See also Jonathan C. Lipson, *Understanding Failure: Examiners and the Reorganization of Large Public Companies*, 84 Amer. Bankr. L. J. 1 (2010) (Prof. Lipson quotes from Bankruptcy Judge Robert Gerber: "[M]andatory appointment [of examiners] is terrible bankruptcy policy, and the Code should be amended...to give bankruptcy judges...the discretion to determine when an examiner is necessary and appropriate...." ;*But see* Clifford J. White III and Walter W. Theus, Jr., *Chapter 11 Trustees and Examiners after BAPCPA*, 80 Am. Bankr. L. J. 289, 290 (Summer 2006) ("If equipped with a mandate of sufficiently broad scope, an examiner may promote efficiency by navigating among the frequent multiplicity of other investigations by government authorities, boards of directors, creditors, and shareholders. The examiner may play the lead role among the players in the bankruptcy case by conducting an expansive and timely investigation that will aid parties later in pursuing monetary recoveries and other remedies. In many respects, the examiner should pre-empt the bankruptcy field by vastly reducing the need for early and duplicative discovery efforts by separate creditors or committees.").

II. DUTIES OF THE EXAMINER

A. Primary Duty is to Investigate

The chapter 11 examiner's role is primarily as an investigator and reporter. The examiner's duties are set forth in section 1106(b) of the Bankruptcy Code:

> An examiner appointed under section 1104(d) of this title shall perform the duties specified in paragraphs (3) and (4) of subsection (a) of this section, and, except to the extent that the court orders otherwise, any other duties of the trustee that the court orders the debtor in possession not to perform.

11 U.S.C. § 1106(b). The duty specified in section 1106(a)(3) is the duty 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. The examiner has the duty under section 1106(a)(4) to report on the investigation performed under section 1106(a)(3). Furthermore, "the examiner answers solely to the court….." *In re Fibermark, Inc.* 339 B.R. 321, 325 (Bankr. D. VT. 2006)

B. Scope of Investigation

The scope of an examiner's investigation is defined by the order appointing the examiner. Some orders are broad. *See, In re DBSI, Inc.,* Case No. 08-12687 (PJW) (Bankr. D. Del.) ("The Examiner is directed to: (a) investigate the circumstances surrounding (i) any and all of the Debtors' inter-company transactions and transfers; (ii) any and all transactions and transfers between and among the Debtors and any non-debtor affiliates, and (iii) any and all transactions and transfers between and among the Debtors and any insiders, officers, directors and principals of the Debtors...."); *In re Washington Mutual, Inc.*, Case No. 08-12229 (MFW) (Bankr. D. Del.) ("The Examiner is directed to investigate ... (a) the claims and assets that may be property of the Debtors' estates that are proposed to be conveyed, released or otherwise compromised and settled

under the Plan and Settlement Agreement ..., and the claims and defenses of third parties thereto ... and (b) such other claims, assets and causes of action which shall be retained by the debtors and/or the proceeds thereof, if any, distributed to creditors and/or equity interest holders pursuant to the Plan, and the claims and defenses of third parties thereto ....").

Other orders directing the appointment of an examiner are broad, but with specific limitations. *See, In re Refco, Inc.*, Case No. 05-6006 (RDD) (Bankr. S.D.N.Y.) ("[T]he Examiner is authorized to investigate and to report all any topic that might reasonably result in the assertion of a claim or right by any of the Debtors' estates with the exception of any claim or right of Refco Capital Markets, Ltd."); *In re Anderson News, LLC*, Case No. 09-10695 (CSS) (Bankr. D. Del.) ("The Examiner shall examine the merits of any and all claims and causes of action held by the Debtor's estate against 'insider[s]'and 'affiliate[s]' . . . of the Debtor . . . , [T]he Examiner shall neither examine nor evaluate the estate's claims against the defendants in that certain antitrust action filed on March 9, 2009, in the United States District Court for the Southern District of New York ....").

Other orders directing the appointment of an examiner are limited to specific transactions or topic areas. *See, In re SemCrude, L.P.*, Case No. 08-11525 (BLS) (Bankr. D. Del.) ("The Examiner is directed to (a) investigate the circumstances surrounding (i) the Debtors' Trading Strategy and the transfer of their NYMEX account, (ii) the Insider Transactions and the formation of Energy Partners, and (iii) the potential improper use of borrowed funds and funds generated from the Debtors' operations and the liquidation of their assets to satisfy margin calls related to the Trading Strategy for the Debtors and certain entities owned or controlled by the Debtors' officers and directors .... "); *In re Enron Corp.*, Case No. 01-B-16034 (AJG) (Bankr. S.D.N.Y.) ("[T]be Examiner is directed to prepare a report regarding the issues concerning [Enron North America Corp.]'s continued participation in the Cash Management System . . . . [and] to participate in both the Cash Approval and Risk Assessment Committees . . . . "); *In re Tribune Co.*, Case No. 08-13141 (KJC) (Bankr. D. Del) ("The Examiner shall . . . evaluate whether there are potential claims and causes of action held by the Debtors' estates in connection with the leveraged buy-out of Tribune that occurred in 2007 . . . "); *In re New Century TRS Holdings, Inc.*, Case No. 07-10416 (KJC) (Bankr. D. Del) ("The Examiner shall: (a) investigate any and all accounting and financial statement irregularities, errors or misstatements . . . [and] (b) investigate any possible post-petition unauthorized use of cash collateral by the Debtor .... ").

C. Court's Ability to Guide and Expand Duties

The court has the ability to guide the examiner's investigation. Section 1106(a)(3) is prefaced by "except to the extent that the court orders otherwise." Furthermore, section 1104(c) directs the court to order the appointment of an examiner to perform such an investigation "as is appropriate." Therefore, courts have significant control over the scope of the investigation. *See UAL Corp.*, 307 B.R. at 86-87.

Significant authority also supports, the court expanding the examiner's duties beyond the required investigation under sections 1106(a)(3) and (4). Specifically, the examiner can perform "any other duties of the trustee that the court orders the debtor in possession not to perform" 11 U.S.C. § 1106(b) (emphasis added). Courts have routinely cited section 1106(b) as authority to expand the powers of an examiner. But a careful reading of the statutory language discloses that

the court's ability to grant the examiner broad, wide-ranging authority is in reality significantly circumscribed.

Although, section 1106(b) allows examiners to perform trustee duties that the court orders the debtor in possession not to perform, it is silent about vesting examiners with rights or powers that are denied the debtor in possession. Efforts to impose upon examiners duties substantially broader than those delineated by the Bankruptcy Code lack solid statutory support and should be viewed with caution. *See Official Committee of Unsecured Creditors v. Chinery (In re Cybergenics)*, 330 F.3d 548, 577-78 (3d Cir.), cert. dismissed, 540 U.S. 1001 (2003).

Despite the lack of solid statutory support and often without thoughtful (or any) consideration of the "other duties" clause and related provisions of the Bankruptcy Code, courts have expanded an examiner's duties to include the following:

- facilitation of communication among the parties;
- holding monthly status conferences to monitor the case;
- coordination of discovery efforts of debtors and committees;
- plan mediation, facilitation and negotiation;
- resolution of disputed claims;
- review and settlement of administrative claims;
- prosecution of claims on behalf of the debtor;
- analysis of tax issues;
- preparation and filing of tax returns;
- handle and control all funds, bank accounts and disbursements of the debtor;
- investigation of the condition of property;
- marketing, negotiation and sale of assets;
- review of proposed agreements, leases, transfers, conveyances, expenditures, payments and transactions to determine whether the debtor should be permitted to engage in such transactions;
- review of proposed transactions between the debtor and affiliates, officers and directors to determine whether the debtor should be permitted to engage in such transactions;
- examination of fees and expenses;
- waiver of the debtor's attorney/client privilege;
- review of debtor's financial viability and recommendation as to whether a trustee should be appointed;
- determination of what financial information should be revealed to parties;

- oversight of debtor's actions with respect to partnerships;
- oversight of creditors' and professionals' negotiations and compliance with court orders;
- exercise of the right to vote on plan confirmation on behalf of partnerships; and
- any and all duties of a trustee.

See The Bankruptcy Court's Watchdog: The Appointment, Role and Power of Examiners Today (published by ABI, 2011). However, in delegating broad powers and duties to an examiner, the bankruptcy court should be mindful of the jurisdictional and constitutional limitations of vesting examiners with expanded powers. *See e.g. City of New York v. Mickalis Pawn Shop, LLC,* 645 F.3d 114 (2d Cir. 2011) (holding that is special master makes significant decisions without careful review by trial judge, judicial authority is effectively delegated to an official who has not been appointed pursuant to Article III of Federal Constitution).

In some circumstances, courts will authorize an examiner to prosecute claims of the debtor, either before confirmation to a plan or pursuant to the plan. However, ordering an examiner to prosecute claims belonging to the estate is difficult to justify under the Bankruptcy Code. The Bankruptcy Code's delineation between the duties and powers of a trustee and the prohibition of an examiner becoming a trustee or being employed by the trustee run counter to appointing an examiner to prosecute claims. Furthermore, commentators frequently recognize as well as courts that the unique and independent role of an examiner suggests that an examiner should not be authorized to prosecute claims. Such an appointment is likely to negatively impact the examiners independence and integrity or the parties and public's perception of the independence of the examiner. *Official Committee of Asbestos Personal Injury Claimants v. Sealed Air Corp. (In re W.R. Grace & Company).*, 285 B.R. 148 (Bankr. D. Del. 2002)

III. DIFFERENCES BETWEEN AN EXAMINER AND A CHAPTER 11 TRUSTEE

An examiner usually has only a couple of a trustee's duties specifically those set out in sections 1106(b)(3) and (4), unless the court orders otherwise. He has none of a trustee's powers and rights. The trustee has a fiduciary duty to creditors and others with interests in the estate. The examiner's duty is to independently conduct an unbiased investigation and to report the results of the investigation to the court and to parties in interest.

The Bankruptcy Code is designed to insure the examiner's impartiality and lack of bias. Like a trustee an examiner must be disinterested. See 11 U.S.C. §§ 1104(d) and 101(14). Likewise, a person who has served as examiner in a case cannot later serve as a trustee in case. 11 U.S.C. § 321(b). This provision eliminates any personal incentive that an examiner might have to advocate that grounds exist for the appointment of a trustee. Finally, and for similar reasons, a trustee is prohibited from employing as a professional a person who has served as an examiner in the case. 11 U.S.C. § 327(f). Although the examiner pursues adequate and detailed knowledge about the case from his investigation, that knowledge should be set out in the examiner's report. Persons dealing with the examiner should be assured that the examiner is a truly independent actor not impaired by personal or pecuniary interests.

IV. THE PROCEDURAL MECHANICS OF THE APPOINTMENT

The appointment of an examiner, like the appointment of a chapter 11 trustee, is governed by section 1104(d) of the Code and Bankruptcy Rule 2007.1. After the court directs the appointment of an examiner, the United States Trustee is required to consult with parties in interest and to then appoint one disinterested person to serve as examiner. During the consultation, the United States Trustee will usually inquire about those persons best suited be considered as potential examiner candidates. The United States Trustee will also seek candidates with the skill sets necessary and appropriate to effectively perform the investigation called for in the court's order.

Once the United States Trustee designates a candidate to serve as an examiner, Rule 2007.1 sets forth the procedures for formalizing the appointment. Under Rule 2007.1(c), the United States Trustee files an application seeking the approval of the appointment. The application will identify the person appointed and, to the best of the applicant's knowledge, all of the person's connection with the debtor, creditors, any other parties in interest, their respective attorneys and accountants; the United States Trustee, or persons employed in the office of the United States Trustee. The application will describe the parties in interest with whom the United States Trustee consulted regarding the appointment. The application will also be accompanied by a verified statement of the person appointed setting forth the person's connections with the debtor, creditors, any other parties in interest, their respective attorneys and accountants, the United States Trustee, or persons employed in the office of the United States Trustee.

The examiner's service begins once the court enters an order approving the appointment. Unlike a chapter 11 trustee, an examiner cannot be supplanted by an election. *See* 11 U.S.C. § 1104(b); Fed. R. Bank. P. 2007.1(b).

V. WORK PLAN AND BUDGET

A court-approved work plan and budget are often required by the appointment order. But see, *Anderson News* (no work plan/budget required by Court). Developing a work plan and budget generally requires cooperation and discussions among parties-in-interest (e.g., United States Trustee, debtor, lender, statutory committees, retained financial advisors) so that the examiner may determine; (1) events that have transpired to date; (2) issues appropriate tor the investigation; (3) the status and progress of any other pending investigations (e.g., SEC, DOJ, Commodities Future Trading Commission); (4) the availability and condition of the debtor's books and records; (5) the extent to which the examiner will need to engage and retain professionals; and (6) other matters likely to affect the investigation.

As discussed below, an examiner is often precluded by the appointment order from making public information regarding his investigation until his report is filed. In many cases, therefore, the work plan and budget may be required to be filed under seal.

VI. EXAMINER'S RETENTION OF PROFESSIONALS

The examiner is generally authorized by the court to retain counsel and other professionals, such as a financial advisor, under standards equivalent to those under section 327 of the

Bankruptcy Code. The examiner and his professionals are typically compensated pursuant to sections 328 and 330 of the Bankruptcy Code and any orders entered in connection with the case in the same manner as other professionals retained in the case. There is no specific authority for these compensation and payment procedure, but court's generally rely on § 105(a) of the Bankruptcy Code.

VII. DUTY OF COOPERATION WITH EXAMINER

Initial orders appointing examiners (or related orders) may require (a) parties-in-interest to cooperate with examiner, (b) the examiner to cooperate in and avoid interfering with ongoing federal, state and local investigations and (c) coordinated discovery process between the examiner's investigation and other Rule 2004 motions by parties in interest.

For example, in *In re WorldCom, Inc.*, No. 02-13533 (Bankr. S.D.N.Y. 2002), in addition to the examiner and Congress, various governmental agencies investigated the debtor as they sought to build civil and criminal cases. A protocol was established to address distribution of information among the various governmental parties:

(1) Criminal prosecutors were given first claim on information. They could decide whether witnesses could speak only to the criminal investigators, or to the SEC and/or examiner as well Criminal prosecutors were also given the right to limit the scope of interviews by others;

(2) SEC was given second claim on all information and the right to protect its civil enforcement action against the premature disclosure of information through the examiner;

(3) It was necessary for parties to ensure certain information was not disclosed to examiner by prosecutors in order to protect grand jury secrecy. This included information developed through grand jury testimony, subpoenaed documents and testimony developed therefrom.

(4) It was also necessary to monitor the information flowing from the examiner to the prosecutors to avoid allegations that the examiner acted as an agent of the prosecutors and that the information was improperly obtained.

In *Anderson News*, an agreed upon stipulation and order was approved governing coordination of a Rule: 2004 discovery process running side-by-side with the examiner's investigation and provided, among other things, various classifications of confidentiality regarding information produced in connection with the examiner's investigation; protocols for disclosure, and the means for separate and simultaneous productions of certain documents to the examiner and various creditor parties.

VIII. BANKRUPTCY RULE 2004 AND SUBPOENA POWER

"An examiner's investigation is conducted under Fed. R. Bankr. P. 2004 and is broader than the scope of civil discovery. The investigation of an examiner in bankruptcy, unlike civil discovery under Rule 26(c), is supposed to be a 'fishing expedition,' as exploratory and groping as appears proper to the Examiner." *FiberMark,* 339 RR. at 324 (quoting *Air Line Pilots Assoc.*

Int'l v. Am. Nat'l Bank & Trust Co. (In re Ionosphere, Inc.), 156 RR. 414, 432 (S.D.N.Y.1993)). The scope of an examiner's investigation, however, is limited to his duties under sections 1104 and 1106 of the Bankruptcy Code, as well as the appointment order. At the outset of the investigation, or as needed during the investigation, an examiner can obtain court authorization to issue subpoenas to, and conduct examinations of, potential witnesses under Rule 2004. Such orders generally serve to limit costs and unnecessary delay.

IX. WITNESS INTERVIEWS BY EXAMINER

Witness interviews generally comprise a significant part of any investigation. Persons with critical knowledge are almost always interviewed in person, often more than once. While examiners often obtain orders granting them subpoena powers, the goal of any investigation is to obtain the best information available in the most effective and efficient manner suitable. For these reasons, it is often the best course for an examiner to forego formal depositions in favor of informal interviews. The use of transcription services may assist the examiner in preserving for later use the content of such interviews and reducing the need for multiple follow up communications. Any such unsworn transcript essentially serves as the examiner's notes and is generally not made available to patties in interest. The use of videoconference and telephonic interviews may be helpful in obtaining cost effective access to persons, particularly third parties, who are believed to have limited or corroborating information regarding the investigation.

Generally, the only persons permitted to be present with a witness at his interview are his counsel and, if the witness is a current or former employee of the debtor, counsel for the debtor.

X. THE EXAMINER'S STANDARD OF REVIEW WHEN ANALYZING CLAIMS

The process of an examiner's work is related to the standard that will be used to evaluate the matters he is assigned to investigate. In at least one case, the court provided guidance regarding the standard to be used by the examiner. See *Report of Anton R. Valukas, Examiner, In re Lehman Brothers Holdings, Inc.*, No. 08-13555 (Bankr. S.D.N.Y, Mar. 11,2010) (noting that bankruptcy court requested examiner to investigate "colorable claims"). In most cases, the standard of review is left to the examiner's discretion. As a result, examiners' reports have not been uniform in the standards employed to evaluate potential claims or causes of action and examiners have run the gamut in selecting applicable standards,

A number of examiners have utilized a standard akin to that governing a motion to dismiss. *See Report of Kenneth N. Klee, As Examiner, In re Tribune Co.*, No. 08-13141 (Ban.kr. D. Del July 27, 2010); *Final Report of Examiner, In re Refco, Inc.*, No. 05-60006 (Bankr. S.D.N.Y. July 11, 2007). Others have employed a heightened standard more analogous to that applied on a motion for summary judgment. See *Report of Anton R. Valukas, Examiner, In re Lehman Brothers Holdings, Inc.*, No. 08-13555 (Bankr. S.D.N.Y. Mar. 11, 2010); *Final Report of Neal Batson. Court-Appointed Examiner, In re Enron Corp.*, No. 01-16034 (Bankr. S.D.N.Y. June 30, 2003). At least one examiner employed a standard in his report intended to set forth claims that would survive both motions to dismiss and for summary judgment. See *Third and Final Report of Dick Thornburgh, Bankruptcy Court Examiner, In re WorldCom, Inc.*, No. 02-13533 (Bankr. S.D.N.Y. Jan. 26, 2004). One examiner adopted a motion to dismiss "plus" standard, concluding tor purposes of his report that a claim or cause of action existed if there were facts sufficient to state a claim

that was facially plausible giving due consideration to the viability of potential defenses that may likely be asserted. See *Report of Don A. Beskrone, Examiner, In re Anderson News, LLC*, No. 09-10695 (Bankr. D. Del. May 12, 2011). Finally, some examiners fail to specifically describe the standard they applied to determine whether claims existed. *See Final Report of Louis J. Freeh, In re SemCrude*, No. 08-11525 (Bankr. D. Del. Apr. 15, 2009); *Final Report of Michael J. Missal Bankruptcy Court Examiner, In re New Century TRS Holdings, Inc.*, No. 07-10416 (Bankr. D. Del. Mar. 26, 2008).

XI. FORM OF THE EXAMINER'S REPORT

Sections 1104 and 1106 of the Bankruptcy Code (hereinafter, the "Code") provide for the appointment of an examiner and set forth the examiner's duties in connection with his or her investigation. The Code further provides that the examiner shall, as soon as practicable, "file a statement of any investigation ..., 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[.]" See 11 U.S.C. § 1106(a)(4)(A).

The Code does not provide any guidance regarding the form or structure of an examiner's report. Most examiners' reports include the procedural background of the case, recite the topics which the examiner was appointed to examine, as set forth in the court's order appointing the examiner, and describe the examiner's investigation, including the documents and testimony collected. Furthermore, a review of examiners' reports filed in recent bankruptcy cases suggests that a report's form and structure is largely left to the examiner's discretion and influenced by the scope of the examiner's investigation.

In *In re Lehman Brothers Holdings Inc., et al.*, Case No. 08-13555 (JMP) (Bankr. S.D.N.Y.), for example, the court instructed the examiner to address ten separate issues relating to certain events and transactions leading up to debtors' bankruptcy filing and the existence of any colorable avoidance actions, administrative claims and state law claims (such as for breach of fiduciary duty) by or against the debtors. In his report, the examiner distilled these ten issues into three primary topics: (i) the reasons for Lehman's failure and the existence of any colorable causes of action arising out of Lehman's failure; (ii) the existence of any colorable avoidance actions or administrative claims; and (iii) the existence of any colorable claims arising out of a sales transaction with Barclays Capital, Inc. The examiner's organization of the report in this manner enabled him to set forth the facts he obtained during the course of his investigation and to provide a detailed analysis of the potential causes of action he believed existed based on those facts.

The examiner in *In re Tribune Company, et al.*, Case No. 08-13141 (KJC) (Bankr. D. Del) was tasked with a similar role, specifically, that of evaluating potential claims and causes of action held by the debtors' estates against various entities. In evaluating the potential claims and causes of action, the examiner constructed a continuum of possible conclusions, ranging from "highly likely" to "highly unlikely," with steps in between. The examiner judged each claim and cause of action according to this continuum, ranking the viability of the claim at issue based on this scale.

In addition to form and structure, the Code likewise lacks guidance with respect to the number of reports that the examiner may file with the court to report the findings of his or her investigation. In some cases, such as *Tribune* and *Lehman*, the examiner only filed a single report.

In other cases, such as *In re WorldCom. Inc., et. al.*, Case No. 02-13533 (AJG) (Bankr. S.D.N.Y.) and *In re New Century TRS Holdings, Inc., et. al.*, Case No. 07-10416 (KJC) (Bankr. D. Del.) the examiner flied more than one report.

XII. SHOULD THE EXAMINER'S REPORT BE PUBLICLY FILED OR FILED UNDER SEAL?

As a general rule, courts appointing examiners and the Office of the United States Trustee (the "U.S. Trustee") have indicated a strong preference that examiner reports be publicly filed. More often than not, however, the time constraints facing examiners prevent resolution of all claims of confidentiality or privilege before the deadline for filing the examiner's report. As a result, to meet the deadline, it is sometimes necessary for an examiner to file his or her report (or portions thereof) under seal until issues related to confidentiality and privilege can be sorted out.

In *New Century*, for example, the order appointing the examiner was supplemented (the "Supplemental Order") prior to the examiner issuing his final report to provide for the report to be filed under seal for at least ten (10) days, with the report being served only upon the debtors, the official committee of unsecured creditors and the Office of the U. S. Trustee (collectively the "Service Parties"). The Supplemental Order authorized the Service Parties to file a motion to keep the report under seal beyond the ten (10) day period to protect disclosure of privileged or confidential information. While the ten day seal period was extended by the court, the report was eventually unsealed.

In *Tribune*, the examiner's court-approved work plan included a procedure for the examiner and his professionals to attempt to resolve claims of confidentiality during the process of the investigation. Despite the examiner's best efforts, approximately fifty-three (53) documents utilized in his report remained subject to claims of confidentiality as of the deadline for filing the report. As a result, the examiner moved to file his report under seal and simultaneously asked the court to overrule the parties' claims of confidentiality and unseal the report. By the time of the hearing on the examiner's motion, most of the parties withdrew their claims of confidentiality and the examiner was authorized to publicly file his report in full.

XIII. USE OF THE EXAMINER'S REPORT

An examiner's report is meant to be a "source of information that assists parties in identifying assets of the estate, evaluating a plan of reorganization, or describing likely and legitimate areas of recovery." *In re FiberMark, Inc.*, 339 B.R. 321,325 (Bankr. D. Vt. 2006). While motions or orders relating to the appointment of an examiner may shed light on the intended use of the report, recent bankruptcy cases illustrate that the ultimate use of the report may differ significantly from the use initially intended by the parties or the court.

The examiner's interim report in *In re DBSI, Inc. et al.*, Case No, 08-12687 (PJW) (Bankr. D. Del.), for example, led to the appointment of a chapter 11 trustee. While the examiner's proposed work plan with respect to his investigation only contemplated the filing of a single and final report at the conclusion of the examiner's four-month investigation, the examiner, during the course of his investigation, determined that an interim report would be appropriate in part because the examiner had uncovered information that brought into question issues concerning the debtors;

books and records and use of cash. The interim report further described the conduct of the debtors' officers and directors with respect to the debtors, its investors and its creditors, and management's misuse of the debtors' funds.

Citing this information, the U.S. Trustee moved for the appointment of a chapter 11 trustee, arguing that the "fraud and misconduct on the part of DBSI's current management constitutes clear grounds for the court to direct the appointment of a chapter 11 trustee under 11 U.S.C. § 1104(a)." The debtors ultimately entered into a stipulation agreeing to a trustee's appointment.

Examiner reports have also been used by parties to provide a blueprint for future litigation, as illustrated by *Lehman*. The examiner's report in *Lehman* concluded that Lehman may have grounds to file litigation against JPMorgan Chase Bank, N.A. ("JPMorgan") and Citigroup, Inc. in connection with Lehman's failure. Following the report's issuance, the liquidating trustee filed suit against JPMorgan and, more recently, Citigroup, Inc., based on factual allegations similar to those set forth in the examiner's report.

Similarly, in *New Century*, both the post-confirmation liquidating trustee and plaintiffs in a securities fraud class action used the examiner's report as a road map for pursuing litigation against the debtors' officers and directors and independent auditors.

A related issue deals with the admissibility of the examiner's report in litigation or other judicial proceedings. In those cases where an examiner was appointed to conduct an analysis of objective issues, or where the examiner's report was not in dispute, courts tended to admit both the examiner's factual findings and conclusions. *See FiberMark*, 339 RR. at 326, and the cases cited therein.

In the face of an objection, however, most courts seem to agree that an examiner's factual findings constitute inadmissible hearsay, but an examiner's conclusions are admissible, with the court to decide the weight afforded such conclusions. See, e.g., *FiberMark*, 339 RR. at 327; *Newby v. Enron Corp. (In re Enron Corp. Securities, Derivative & "ERISA" Litig.)*, 623 F. Supp. 2d 798, 823 n.21 (S.D. Tex. 2009) (stating that examiner was an "extremely qualified expert in bankruptcy" and thus his conclusions and opinions were admissible as expert opinion in determining the defendants" liability). *But cf. In re Baldwin-United Corp.*, 46 B.R. 314, 316 (Bankr. S.D. Ohio 1985) (stating that an examiner's report does not "have the evidentiary character of an opinion by a Court expert" appointed under Fed.R.Evid. 706). As stated by the *FiberMark* court, "[i]n essence, an examiner's report paints a picture, his or her image of what happened in the case, and ends with that expert's opinion of what that story means, in legal terms. The report puts the story on paper and provides a context for debate. It is the duty of the parties to formulate a fuller version of the debate using the rules of evidence." *FiberMark*, 339 B.R. at 325.

A notable exception to the cases cited above is *In re Washington Mutual*, Case No. 08-12229 (MFW) (Bankr. D. Del) ("WaMu"), in which the court excluded the entire examiner's report from admission at the hearing on confirmation of the debtors' proposed plan. In *WaMu*, the court appointed an examiner to review; among other things, a settlement agreement underlying WaMu's then-proposed reorganization plan, between WaMu, JPMorgan and the Federal Deposit Insurance Corporation (the "FDIC"). The settlement resolved lawsuits by and between those entities involving the ownership of about $4 billion in disputed deposit accounts and entitlement to

received and expected tax refunds resulting from WaMu's operating losses. The settlement also included a complete release of claims against JPMorgan and the FDIC by WaMu, its shareholders and creditors. The Official Committee of Equity Security Holders (the "WaMu Equity Committee") objected to the proposed settlement and requested the appointment of an examiner, arguing that investors needed to know the potential value of the company's assets and the potential claims that were released under the proposed settlement to determine whether the settlement was fair and in the best interests of the estate.

An examiner was appointed, conducted an investigation, and filed a report concluding that the proposed settlement "reasonably resolve[d] contentious issues" and was not made in bad faith. The examiner's report further provided that any further litigation would be "highly unlikely" to recover more for shareholders and, instead, would "essentially result ln gambling with currently guaranteed recoveries to unsecured creditors in order to attempt to obtain speculative recoveries for shareholders and other 'out of the money' claimants."

Parties in other cases have entered into stipulations resolving issues regarding the admissibility of an examiner's report. For instance, in *Tribune*, the patties stipulated to the use and admissibility of the examiner's report during the confirmation hearing. In pertinent part, the parties agreed that: (i) the examiner's opinions would be admissible by any entity for all purposes to the same extent as the opinions testified to by an expert witness under the Federal Rules of Civil Procedure; (ii) the examiner's opinions would not be binding on the court or any entity, nor would there be a presumption of correctness attributed to such opinions; and (iii) all entities would have an opportunity to state and describe their agreement or disagreement with any of the examiner's opinions in their confirmation briefs and to submit appropriate evidence and/or expert testimony in support of their positions during the confirmation hearing.

XIV. DISCHARGE OF THE EXAMINER

At the conclusion of an examiner's investigation, and after a report is filed, the examiner typically files a motion for an order discharging the examiner and granting other, related relief (a "Discharge Motion"). These motions and subsequent orders (a "Discharge Order") typically contain the following provisions:

- Discharge: A Discharge Order typically will state that the examiner is discharged from any commitments or representations with respect to his duties as examiner.

- Cooperation: A Discharge Order often will require an examiner to cooperate with other parties in the case, particularly in responding to requests for information regarding the examiner's investigation. In Tribune, for example, the Discharge Order provided that the examiner would respond to "reasonable written inquiries" from the parties concerning documents received, maintained or created during his investigation. As discussed more fully below, a Discharge Order typically will place limits on third-party discovery directed to the examiner or his/her professionals.

- Payment of Fees: A Discharge Order typically provides for the reimbursement of the examiner and the examiner's professionals for their reasonable fees and actual costs after the date of discharge for, inter alia, the disposition of documents obtained during the course

of the investigation, responding to discovery requests authorized by the court and preparing and prosecuting fee applications.

- Release: A Discharge Order typically will Include provisions addressing the exculpation of an examiner and his/her professionals. These release provisions generally are broad, providing for the release of the examiner and his/her professionals from any and all liability with respect to any act or omission, statement or presentation arising out of, relating to, or involving in any way, his/her investigation or any report, pleading or other writing filed by the examiner in connection with the bankruptcy cases, except in the case of gross negligence or willful misconduct.

- Disposition of the Investigative Record: A Discharge Order also may address the disposition of the examiner's investigative record (consisting of all documents he or she has gathered and/or prepared during the course of the investigation) as of the date of discharge.

    - In *Lehman*, for example, the Discharge Order required the examiner and his professionals to transition the maintenance of a database of documents compiled during the investigation to a neutral vendor that would undertake custody of and maintain the database,

    - Similarly, in *Tribune*, the examiner was authorized to transfer both his report and the non-confidential documents comprising his investigative record to the debtors; claims agent, which would maintain the documents at the debtors' expense and provide public access to same. The examiner, in turn, was required to maintain the complete record (including privileged materials) for a period of two years following his discharge.

While the respective examiners' dispositions of the investigative records in *Lehman* and *Tribune* were relatively non-controversial, the issue raised concerns and elicited objections in *New Century*, where the disposition of the investigative record, as requested by the examiner, prompted questions regarding the neutrality of an examiner.

The court ultimately granted the examiner's request for authority to transfer portions of the investigative record) including certain materials claimed to be privileged or confidential, to the liquidating trustee. The court reasoned that allowing the transfer of these materials was not inconsistent with the protective order previously entered relating to these materials, but instead furthered the purpose of the order in preventing the bankruptcy estate from having to pay twice for the same investigation in pursuit of potential claims.

The court denied, however, the examiner's request for an order providing that his sharing of documents with governmental agencies, the U.S. Trustee and the liquidating trustee failed to constitute a waiver of any applicable protection or privilege, leaving that issue for another day, and perhaps, another court.

XV. THIRD-PARTY DISCOVERY OF THE EXAMINER

An examiner is an independent third-party and an officer of the court, whose role is disinterested, non-adversarial, and investigative in nature. See *Baldwin*, 46 B.R. at 316-17; see also *In re Big Rivers Elec. Corp.*, 213 B.R. 962, 977 (Bankr. W.D. Ky. 1997) (recognizing the examiner is an independent third-party and an officer of the court). The examiner is a fiduciary only to the court, and not to other interested parties and does not "act as a conduit of information to fuel the litigation fires of third-party litigants." *Baldwin* 46 B.R. at 316. As such, an examiner is generally not subject to civil discovery and courts have held that an examiner's investigative file is not a judicial record and that there is no right to public access of same. See *Air Line Pilots Ass'n. Int'l v. Am. Nat'l Bank & Trust Co. (In re Ionosphere Clubs, Inc.)*, 156 B.R 414,435 (S.D.N.Y. 1993), aff'd, 17 F.2d 600 (2d Cir. 1994) ("The public interest is in the Report and the Examiner's conclusions, not in the Record upon [which] the conclusions are based.").

An examiner typically will request protection from third-party discovery of both himself and his professionals as part of his Discharge Motion and the court typically will include such a provision in the Discharge Order. In general, such provisions preclude any creditor, party-in-interest in the particular bankruptcy case, or third-party from issuing or serving formal or informal discovery requests on the examiner or his/her professionals relating the debtors, the bankruptcy case, or the examiner's report, appointment, or investigation. Furthermore, the Discharge Motion will typically request and the Discharge Order permit discovery requests upon the examiner and his/her professionals only if: (i) requested by order of a federal district court in the context of a criminal proceeding pending before that court; or (ii) the party requesting such discovery cannot obtain the requested documents from any other source, production would not violate any order of the court, and the documents requested are not privileged.

XVI. BENEFITS AND DETRIMENTS OF AN EXAMINER

A. Benefits of an Examiner

Many examiner motions advance alternative grounds for relief in motions for the appointment of a chapter 11 trustee. Often these are filed by the United States Trustee early in the case, particularly when there are reasonable grounds to suspect that management has engaged in fraud, wrongful acts or other misconduct. See 11 U.S.C. § 1104(e). A party moving for a trustee will frequently face an uphill struggle, Some courts have raised the burden of proof on trustee motions to a "clear and convincing" standard. Much of the evidence is under the control of the debtor. The debtor will often claim to have replaced the bad actors in its management, and therefore that any pre-petition misconduct that occurred was not performed by "current management," as required by section 1104(a)(1). But an investigation is still necessary to assure that all wrongdoers have been identified and that the scope of the pre-petition misconduct is fully established, and often an independent examination by a highly-qualified examiner can help clear the air and free the parties to begin to work toward a plan while knowing that a thorough investigation is underway,

In recent years, parties have increasingly sought the appointment of mandatory examiners to investigate issues that have arisen after the filing of the case, These issues include valuation of estate assets, violations of the debtor's fiduciary duties by negotiating deals that are detrimental to the interests of one or more constituencies. The movants will claim they need the assistance of an

examiner to discover the truth about what is happening in the case. The debtor will claim that the movants are overly aggressive adversaries seeking to derail the plan confirmation process and to exact unfair concessions from others in the case. Because the issues underlying an examiner motion filed on the eve of confirmation would likely form the basis of objections to the plan, the court may consider hearing confirmation first. If the court concludes that the objections lack merit, confirmation of the plan will moot an examiner motion because an examiner cannot be appointed post-confirmation. Otherwise, the court can deny or delay confirmation and direct the appointment of an examiner to provide an independent review of the issues raised in the objections.

B. Detriments of an Examiner

Tensions often arise between examiner and parties-in-interest regarding the range of substantive and procedural issues to be addressed by the examiner. For example, if creditor parties are permitted to undertake or continue Rule 2004 examinations or other discovery during the pendency of the investigation, such parties may attempt to have the examiner pursue their prerogatives. While in some cases such parties and the examiner may share a common interest in obtaining similar types of information, there may be instances in which common ground does not exist, such as where creditors are parties to pending litigation with the debtor. It should always be remembered that the examiner, as an objective and disinterested person, has goals distinct from those of any particular creditor or party in interest, Similarly, creditors may feel that the investigation is not progressing as quickly as they would like and may seek to compel the examiner to press the investigated parties for expedition. The debtor and/or investigated parties may have issues with the reasons the examiner is pursuing certain information or the methods employed. Disputes regarding such issues that are not capable of informal resolution, are most appropriately raised with the court because that is the source of the examiner's charge. Additionally, it should be noted that the cost of the investigation has been the source of tension between the examiner and parties in interest in certain cases.

C. Best Practices for Examiners

At the conclusion of his appointment as examiner in the Lehman bankruptcy cases Anton R. Valukas detailed for the United States Trustee's office his recommendation as to the best practices for examiners. Attached is a copy of the letter sent by Mr. Valukas to Diana Adams, United States Trustee summarizing his recommendations.

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April 1, 2010

Via E-mail and US Mail

Diana Adams
United States Trustee
Office of the United States Trustee
33 Whitehall Street, 21st Fl.
New York, NY 10004

Re: Best Practices for Examiners

Dear Diana:

When I undertook my appointment as Examiner in the Lehman bankruptcy, you and Cliff White asked that I report, at the conclusion of my investigation, on suggested best practices that might assist future Examiners perform their work. The Lehman examination was, of course, unique to Lehman; and given its size and scope, practices that worked for Lehman may or may not translate to other examinations. But I offer the following observations.

Initial Steps

Recommendation 1: New Examiners should speak with and review the reports of former Examiners to learn what worked in prior assignments.

The recommendations that follow are not simply mine. As I embarked upon this process, I began by speaking with other Examiners who had served in major proceedings, precisely to get a sense of best practices before I formed my own work plan. I spoke with Richard Thornberg (Worldcom), Neal Batson (Enron), and Josh Hochberg (Refco), and I was greatly assisted by their input. I reviewed the reports filed by those Examiners, and by others, in great detail, to see how they organized, conducted and reported upon their own investigations. All of that was enormously useful and future Examiners should build on our collective experience.

Recommendation 2: If the Court has not imposed a timetable for the Report, the Examiner should give himself and his team the discipline of a deadline.

The Lehman matter was especially challenging, given the scope of my assignment and the size of the universe I was asked to explore. It was apparent that our factual investigation would require hundreds of witness interviews. The volume of Lehman documents alone was estimated to amount to close to half a trillion pages; and relevant documents resided not just at Lehman but with dozens of third parties. Added to the magnitude of the work was the limit of time. Although the Court did not impose any deadline for the completion of my Report, I was keenly aware of the exclusivity date for the Debtors to suggest a plan and the fact that the value of my Report would be greatly enhanced if I were able to deliver the Report prior to that date.

My team and I ultimately reviewed more than thirty million pages of documents and interviewed more than 250 witnesses; we produced a comprehensive Report and filed it within thirteen months of my appointment. We could have done more work. We had collected millions more pages we might have reviewed; we had billions more pages we might have requested. We had identified hundreds more people we might have talked to. We might have circled back and re-interviewed each of the 250+ persons we had already talked to. But the fact is that doing that additional work might in theory have added marginally to the final product, while the stark reality is that to do so would have come at an unreasonable cost, both in dollars and time. I set a deadline and adhered to it; and the process was better for that.

Recommendation 3: The Examiner should enlist, accept, and use the aid and cooperation of the community.

I have said this before, and I emphasize it again here. My Report could not have been filed as expeditiously as it was without the genuine assistance and cooperation my team and I received from nearly every constituent in the Lehman community.

My order of appointment required that I meet with the interested parties. I would like to think that I would have had the good sense to do exactly that even if the Court had

not had the wisdom to have ordered it, because those meetings were extremely helpful.

By the time of my appointment, the Debtors, the Creditors Committee, and other parties had assembled documents and performed analyses. We asked for – and were provided access to – all of that work product.[1]

The Debtors, the Creditors Committee and the interested parties were and are represented by the cream of the New York and National bars. These excellent lawyers had excellent suggestions, and our conversations with the parties provided real guidance to steer the investigation. Other Examiners could benefit as I did by seeking out and listening to the parties.

That said, while it is important to seek suggestions and guidance from the parties and their counsel, it is critical that the Examiner maintain independence and objectivity.

Recommendation 4: The Examiner should perform every task necessary to produce a complete report; but do each task once, and do it right. That said, there is utility in doing some early interviews even before document production is complete.

We were eager to begin witness interviews immediately. We needed, of course, to first collect and review documents. But there were exceptions. One of the suggestions made by other Examiners was that a few key interviews – even before document production – could be very useful to inform issues and suggest the direction of the investigation.

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[1] While I am sincere in my praise of the parties' cooperation, I don't want to overstate its contribution to the final Report. I have also said this before: we had hoped that the parties' document collection and analysis, by the time of my appointment four months after the bankruptcy filing, would have been more mature and complete than it turned out to be. Because it was not so, I had to extend the projections I had made for completion of my work. But the fact remains that it is a good practice to feed off the work of others wherever possible.

We identified a relatively small number of key witnesses to interview even though document production was in its infancy. In general, those early interviews were with persons who (1) would help inform us on overriding issues and (2) would be available and willing to submit to further interviews after document review. And the other Examiners were right – these initial, early interviews did greatly assist the direction of the investigation.

Organization of the Team

Recommendation 5: The Examiner, of course, needs to assemble the right team for the task and organize it efficiently.

Every examination will be different and the manpower and organization needs will vary accordingly. But let me set out what did work for me and this matter as a guide for others.

It was apparent that this matter would require the almost full-time participation of scores of lawyers and financial professionals. Organizing them, coordinating their efforts, and avoiding redundancies and waste would present challenges.

First, we analyzed the 10 issues that had been assigned to me in my order of appointment and sorted them into four substantive areas. Five teams were created – four substantive teams and one administrative team which exercised oversight and coordination.

Second, we assembled a group of senior lawyers as team leaders with backgrounds and experience as trial lawyers, former prosecutors, bankruptcy lawyers, securities specialists and corporate lawyers. Each team was then staffed with other lawyers as necessary. As you know, Bob Byman served as my lead attorney, basically as chief of staff. It was his job to coordinate the activities of the five teams.

Third, each team was required to develop a work plan for my approval, so that they and I had a shared understanding of what work they proposed to do and by what deadlines. The work plans were shared among all of the teams so that we could reach consensus that nothing was overlooked but that nothing was being done twice. The work plans from each team listed the documents they wanted to collect, the search

terms to be used for collection, and the parties from whom to request documents. The work plans listed the witnesses each team proposed to interview and the anticipated order and dates for interviews. Of course, there were many witnesses listed by multiple teams; Bob would coordinate which team would take the lead for individual witnesses.

Fourth, each team prepared and periodically updated an annotated proof outline of its anticipated sections of the Report. That way, we were able to see early on what areas were covered, what areas remained for planned fills, and whether there were any holes that needed to be plugged.

Fourth, we asked Duff & Phelps, my financial advisors, to organize themselves similarly so that each legal team would have counterparts – dedicated advisors focusing on specific issues. To minimize unnecessary expense to the estate, Duff was asked to periodically list for us each deliverable they had been asked to perform, including the team which had made the assignment and the expected delivery date. Duff was instructed that it was not to perform any tasks unless they were reported on the deliverables list.

When we identified areas which required education on topics that even great lawyers might not be intimately familiar with – topics such as credit default swaps or derivative trading or FAS 157 accounting – we had Duff prepare and give us tutorials. We offered the same tutorials to the government as part of our cooperation with them (see below).

Fifth, we had regular communication among and within teams to ensure that teams and sub-teams did not develop silo mentalities, at the same time avoiding redundancy as much as possible.

Fee examiners in run of the mill cases typically react negatively to billing entries that show inter-office meetings. This was not a run of the mill event. As the investigation unfolded, hundreds of thousands of documents were reviewed daily; multiple witnesses were interviewed each day. Individual witnesses and documents did not usually fit neatly within a single team's responsibility. It was critical that every team knew what every other team was finding in real time.

We held weekly team leader meetings; key documents were circulated to all team leaders as they were found; interview summaries were circulated to all team leaders as they were prepared. We decided that all team leaders needed to be kept as informed as possible about daily events; each team leader exercised discretion as to whether and to what extent to pass on information to team members.

Government Coordination

Recommendation 6: Government coordination is essential, and best accomplished by regular, agreed protocols.

My order of appointment, of course, required that I cooperate with government agencies that may have an investigative interest in Lehman; but even if I had not been so ordered, cooperation was essential lest the government decide to block or shut down an area of my inquiry.

I initially met with the SEC and representatives of the US Attorneys for the Southern and Eastern Districts of New York and the District of New Jersey. After the initial face to face meetings, we held weekly conference calls for most of the period. We had several other face to face meetings.

We established several protocols that made the process agreeable to the government, so that they did not feel a need to restrict my investigation.

First, we agreed to clear with them any witness before we took an interview. We sent our proposed list of witnesses to the government periodically; after a default period of time (generally 5 business days) without express reservation, we would then be free to schedule an interview. Once scheduled, we would give the government notice of that, so that they had another opportunity to ask us not to interview a particular individual. We asked the government to advise us if there were any questions or subjects they wished us to address in interviews. Over the course of the investigation, the government did ask us to defer speaking to a number of individuals; but eventually, they released us to speak with every person we requested.

Second, we kept the government informed in real time of the significant facts we were developing. Our communications were, as these things almost always are, one way.

In our weekly calls, we would debrief the government on key information or documents as we learned it.

Third, as mentioned above, we made Duff available – as well as our lawyers who became expert in areas such as Repo 105 – to give the agencies tutorials on subjects they might not be totally familiar with.

Cooperation with the government, of course, includes our interaction with your office. We need not describe to you what that interaction was, but I hope you agree that I achieved my goal to keep you appropriately informed without overly immersing you in unnecessary detail.

Document Collection and Review

Recommendation 7: The Examiner should get – but try not to have to use – Rule 2004 Subpoena power.

Within weeks of my appointment, I filed a motion asking that the Court grant me expansive Rule 2004 subpoena powers. It was important to have subpoena power; and it was equally as important not to have to use it. Having the power gave my lawyers the leverage to negotiate voluntary production on a much faster track than formal process would have provided.

It was also important that the parties knew I would use the power if pressed. There was a single party which did not voluntarily in timely fashion produce the documents we requested. We issued a subpoena to that party and teed up a motion to compel for the Court; and the party decided to produce rather than fight the subpoena. With the exception of a few other instances where a producing party *requested* a subpoena, we were not otherwise required to use formal process or the Court's assistance to get the documents and interviews we sought.

The document experience carried into the way we conducted interviews, which I describe in detail below. But in all areas, the point is that the Examiner's role is investigative but not adversarial. It is necessary to get the facts, to ask the hard questions, to press for complete production. But it is not necessary to do so with an adversarial tone; it was my experience that we achieved full and complete production

far more quickly by adopting a cooperative tone than we would have through a formal subpoena process.

Recommendation 8: The Examiner will likely be asked to agree to confidentiality stipulations to get documents; he should agree, but perhaps with a standard order.

Nearly every producing party requested confidentiality agreements during document production. As part of the cooperative process, I agreed to any reasonable request for such agreements rather than take the time to negotiate or argue. In retrospect, this is the one area in which I might have acted differently than I did. We ended up with 16 different formal agreements and 5 different informal undertakings. It turns out that only a single agreement has come to issue – our relatively minor dispute with the CME over the publication of three documents. But if there had been more disputes, the Court and I would have had to sort out all of these different agreements with slightly different terms. If I had it to do over, I might have asked the Court to approve a single form of protective order to govern production from all parties.

Recommendation 9: The Examiner should use contract attorneys where possible to conduct document review.

As you know, we used contract attorneys to the fullest extent practicable to do first level document review. We had as many as 70 contract attorneys working at the same time, and our experience with them was excellent. We estimate that the savings to the estate, over the rates that would have been charged by Jenner associates, was in the tens of millions of dollars; moreover, we could not have deployed 70 additional, full time Jenner lawyers without a substantial time lag – the whole process would have taken much longer without the use of contract attorneys.

Recommendation 10: But substantive review must be done by lawyers who are fully integrated and invested.

We do not want to suggest that contract attorneys should have been used to an even greater extent than they were. As a group, the contract attorneys performed very well for first level review – that is, the initial screening of a data dump to identify documents of possible substantive interest. All second level review was performed by Jenner

lawyers. Our experience was that most of the contract attorneys did not have the skills, background and commitment to do effective and efficient second level review.

Jenner lawyers supervised the contract attorneys and exercised quality control. Jenner lawyers who did document review were fully integrated into the substantive teams so that they actually knew what to look for and so that they were able to make more refined searches to locate key documents more quickly.

Recommendation 11: The documents should be collected and maintained so as to make them an asset of the estate.

Our document collection and archival was conducted by seasoned trial lawyers who know how to try cases. As a result, the data base we have assembled is, as it should be, a valuable asset of the estate to limit costs in any pending and future litigation.

Many lawyers are familiar with document management systems such as Concordance which have served them in the past. But we recognized early on that those usual systems would not be up to the task of handling the quantities of documents we would assemble. We involved IT personnel at the outset to ensure that we had the right systems, and opted to maintain our document repository on two extremely robust, easy to search systems, CaseLogistics and Stratify.

The numbers are staggering. We extracted roughly 35 million pages of documents from Lehman's systems – an enormous amount of material, yet only one tenth of one per cent of the universe of Lehman's electronically stored data. We used carefully refined searches so that we would not be overwhelmed with returns. We kept careful records of the search terms we used, the date ranges of the searches, and the custodians against whom the searches were run. Those searches need not be rerun; the parties can look at our searches and add focused additional searches if necessary to their specific needs, but they need not reinvent our wheel. We have assembled the collected documents into electronic, searchable format, so that parties may pull what is relevant to them.[2]

Witness Interviews

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[2] Protective order issues still remain before free public access can be granted, but the documents are assembled; that substantial work need not be done again.

Recommendation 12: The Examiner should consider using informal interviews in most cases.

As you know, one of the suggestions made to me by other Examiners – which I adopted – was that wherever possible interviews be conducted informally, without requiring that the witness be sworn and without transcripts. There are obvious pros and cons. Even had I used transcribed statements under oath, they would have no evidentiary value in pending or future litigation, so the real advantage of oath and transcription is that a quotation of a witness's testimony can be precise. But my team of seasoned litigators estimated that it could easily double the amount of time take interviews with transcription; it would add significant cost; and, significantly, we anticipated that witnesses would be far more likely to be open and candid in an informal setting than if a reporter was transcribing each word. Moreover, the creation of transcribed statements might have impacted pending Government investigations and the government's willingness to release persons for interview.

Balancing these factors, I decided to use informal interviews wherever possible – and that turned out to be possible in all cases. As I noted above in the document collection process, our tone was investigative rather than adversarial. The informality of the interviews was a definite aid. We asked the tough questions where we had to; but the informal setting and objectivity we brought to the process made the witnesses comfortable to fully answer our questions.

To assure accuracy, all interviews were conducted by at least two attorneys, one of whom was assigned to keep careful notes. Flash summaries were prepared as soon as possible, usually the day of the interview, and reviewed by all lawyers present while recollections remained sharp; and full summaries were made and reviewed as soon as practical after that.

Recommendation 13: The Examiner should make the interviews an open book, not an occasion for cross-examination.

Prior to each interview we provided advance notice of the topics we intended to cover and advance copies of the documents we anticipated showing the witness. That procedure would have been anathema to a litigator – but, again, my goal was to get the

facts, not to surprise a witness into some admission. By giving advance notice, witnesses were able – and expected – to refresh recollection before the interview rather than on the fly. That greatly reduced the need for follow-up interviews. It put the witnesses and their counsel at ease that we were not trying to trap.

A number of the parties – including nearly every party against whom I reported colorable claims – have expressly told me that while they might disagree with my conclusions, they were satisfied with the process. I commend that process to future Examiners.

Recommendation 14: Interview outlines should be shared among teams.

In general, detailed interview outlines were prepared at least a week in advance and circulated among team leaders so that all substantive teams could have input on each interview. Moreover, having the outlines prepared in advance allowed us to identify the topics to counsel for the interviewee as described above.

Recommendation 15: The Examiner can supplement or supplant interviews with written questions.

In all, my lawyers and I interviewed more than 250 individuals. There was only one individual I sought to interview but could not – Hector Sants, chief executive of the UK's Financial Services Authority ("FSA"). However, the FSA did provide detailed, written answers to specific questions that would have been posed to Mr. Sants, and while not perhaps as satisfying as an interview, they sufficed.

In other cases, letters to interested parties' counsel with fairly discrete questions to confirm key background facts proved very helpful. For example, we asked a clearing bank to confirm that we had set out in a written question a comprehensive list of all collateral calls made in a particular period. The written exchange was more efficient than Q&A in an interview.

The Report

Recommendation 16: Examiners should carefully define terms not defined in their orders of appointment.

My order of appointment asked me to opine on the existence of colorable claims but did not define that term. The Second Circuit has described colorable claims as ones "that on appropriate proof would support a recovery," "much the same as that undertaken when a defendant moves to dismiss a complaint for failure to state a claim."[3]

I was mindful of the fact that there is a high likelihood that an actual claim will be asserted wherever I have concluded that a colorable claim exists, so I was reluctant to adopt a motion to dismiss standard. Having conducted an extensive factual investigation, I felt it was appropriate to use a higher threshold standard, and therefore defined "colorable claim" as one for which I found sufficient credible evidence to support a finding by a trier of fact.

In addition to defining terms, I recommend that future Examiners do something early on that I did somewhat late. Appendix 2 to my Report is a 98 page glossary of defined terms, names, acronyms and phrases; without that glossary and the ability to use abbreviations for defined terms, the Report would have been cumbersome and unwieldy. I did not append another document that was created during the writing process – a set of protocols that collectively amounts to our own private Blue Book of Citations. Although there were many individuals who contributed first drafts of sections, the overall Report was carefully edited to conform to the Glossary and Blue Book, resulting in a uniform style and appearance. That is not merely cosmetic; I believe that it greatly enhanced the readability of this lengthy tome.

But I confess that we came a little late to the realization how useful the Glossary and Blue Book would be. The editing process would have been less a challenge had we begun assembling and circulating those documents to the substantive teams before first drafts were created.

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[3] *In re STN Enters.*, 779 F.2d 901, 905 (2d Cir. 1985); *In re KDI Holdings, Inc.*, 277 B.R. 493, 508 (Bankr. S.D.N.Y. 1999).

Recommendation 17: The Report should contain as much detail on the claims that are not found as it does for claims which are found.

We devoted as much time and energy to conclude that claims did not exist as we did to conclude that there were claims. And we devoted almost as much space in the Report to those non-claims as we did to the claims.

I felt it was important that the Report set out the detailed facts that led me to conclude the absence of claims so that the parties can use that analysis to make measured judgments whether to expend their own time pursuing claims I have concluded are not there.

Recommendation 18: Examiners should consider whether persons against whom the Examiner tentatively determines there are colorable claims should be given an opportunity to supplement the record.

After I made tentative determinations as to colorable claims, I decided to give each such person and entity an opportunity to present additional factual detail they thought might dissuade me. I stressed that I was not looking for a *Wells* submission, but simply additional facts that I might not have had in making the initial determination. Every identified party took me up on the offer and presented additional materials.

I should stress that I perceived no obligation to go through that procedure, and I do not recommend that any such procedure be used in all Examiners' investigations. I simply note that under the unique circumstances of my investigation, the process worked; it had a real impact upon reaching fair and reasoned judgments. Future Examiners should consider whether it might work for them.

* * * * * *

Diana, it has been my great honor and privilege to have served as Examiner in this matter; thank you again for the trust you showed in me and our firm. I hope that this is useful to you; and I stand ready to assist in any further way I can.

Sincerely,

Anton R. Valukas

cc: Robert L. Byman

IV. Receivers.

A. Rhoades

[Receivers section follows. (17 pages)]

Receiverships, Another Chapter

By

C. David Rhoades, CFE, CTP, CFC

Presented to the Tenth Circuit Fellows of the American College of Bankruptcy

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Receiverships, another Chapter.

The concept of Receiverships dates back well over 150 years. The case law, much of which was promulgated by the United States Supreme Court laid a foundation that has remained solid to this day. In this paper, I will give the applications that have been used to operate Receiverships and that can be used today as an alternative to utilizing the Federal Bankruptcy Courts.

Receiverships can be either under Federal or State jurisdiction. In my practice of doing nearly 200, Federal cases only comprise about 5% of those filed. Regardless of the jurisdiction, the basics are governed by the state law. I will explore the operations of a Receivership and the case law that sets forth the rules for the operations.

Because much of the case law and statutes are state related, and since my experience is primarily in Oklahoma, I will support my concepts with Oklahoma law. 12 O.S. §§1551 – 1554, see Exhibit A. As you can see, there is very little statutory law the governs Receiverships in Oklahoma. There is a high probability that the other states will have comparable case law and statutes that can be applied, as we have in Oklahoma.

It is paramount to get an Order Appointing Receiver that defines as many variables as possible. At least under Oklahoma law, the scope for the Receivership Estate and the power of the Receiver is functionally unlimited as long as the Order Appointing Receiver dictates the guidelines. The scope and powers are outlined herein:

1. A Receiver is Independent. Although usually nominated by a creditor, a receiver can be appointed *sua sponte*. The parties must understand the relationship between all of the stakeholders. The Receiver works for the Judge and the Judge alone. This creates an independent party for a situation in which the parties usually are adverse. These cases support this relationship:

a) A receiver is not an agent of a receivership's creditor, and, thus, statements by the receiver cannot be imputed to the creditor. *See Atlantic Trust Co. v. Chapman*, 208 U.S. 360, syllabus (1908) ("The receiver is not the agent of the plaintiff in the

litigation nor does the plaintiff have any control or authority over him . . . ."); 12 C. Wright, A. Miller, & M. Kane, Fed. Practice and Proc., § 2981, at 9-10 (2d ed. 1997) (A receiver "is . . . not an agent of the parties."); Actions of a receiver cannot be imputed to a party in the receivership action. *In re Phillips*, 24 B.R. 712, 714 (Bankr. E.D. Cal. 1982) ("The receiver is not the agent of the plaintiff nor . . . acting on the plaintiff's behalf or under his control.").

2. Judicial Immunity. A Receiver must be able to do their job without the threat of intervention. It is inevitable that the parties will attempt to influence the decisions that the Receiver makes and when they are unsuccessful, the threats begin. With judicial immunity, the Receiver is protected by this shield and can do their job. The Courts have reinforced this concept.

a) The case of *Hathcock v. Barnes*, 25 P.3d 295, 296 (Okla.Civ.App. 2001) cited with approval the Oklahoma Supreme Court case of *Farrimond v. State ex rel. Fisher*, 8 P.3d 872, 876 (Okla. 2000) which noted "a court-appointed receiver acts as a functionary of the court and as such is performing a judicial act. Thus, immunity is justified and defined by the functions it protects and serves, not by the person to whom it attaches". *See also, Teton Millwork Sales v. Schlossberg,* 311 F. App'x 145, 150 (10th Cir. 2009) ("a court-appointed receiver has absolute quasi-judicial immunity if he is faithfully carrying out the appointing judge's orders.") (citation omitted).

3. Business Judgment Rule. As a Receiver, one cannot always 'get it right' even with Court approval of the major decisions. It has been recognized that in a fiduciary capacity, a Receiver has to do the best they can with what they have to work with. It is important when considering a candidate for appointment, that you attempt to find someone that has some relevant experience, where their decisions have a better chance of success. This does not mean industry specific, although that helps, but does mean that a broad range of experience is necessary. An example of this is:

a) Although there appears to be a dearth of federal common law on this topic, Oklahoma courts have also long recognized that a receiver's decisions regarding the management and operations of property within his control are subject to the business judgment rule. *See Harris v. Dildine*, 251 P. 76, 77 (Okla. 1926), ("A receiver is vested with discretion to manage and control the property entrusted to him in such manner as an ordinarily prudent business man would manage and control his own property.") (Internal quotation marks and citations omitted). "[R]eceivers, just like corporate directors, are entitled to the deference of the business judgment rule in their decision-making concerning the management of a corporation." *Golden Pac. Bancorp v. F.D.I.C.*, No. 95 CIV. 9281 (NRB), 2002

WL 31875395, at *9 (S.D.N.Y. Dec. 26, 2002), *aff'd sub nom. Golden Pac. Bancorp. v. F.D.I.C.*, 375 F.3d 196 (2d Cir. 2004).

4. Authority. In addition to the state statutes and case law, there is some Federal support for the receivership process. Examples are:

a) Federal Rule of Civil Procedure 66 and federal common law support the appointment of a receiver. The 11th Circuit Court of Appeals held in the case of *National Partnership Inv. Corp. v. National Housing Development Corp.*, 153 F.3d 1289 (11th Cir. 1998) at pages 1291-1292:

> As the First Circuit noted in Chase *Manhattan Bank, N.A. v. Turabo Shopping Center, Inc.*, 683 F.2d 25, 26 (1st Cir. 1982), "[m]ost federal court decisions dealing with the appointment of a receiver pendente lite appear to apply federal law without discussion." Of those circuits that have directly addressed the issue, each has held that the appointment of a receiver in a diversity action is governed by federal law. *See Aviation Supply Corp. v. R.S.B.I. Aerospace, Inc.*, 999 F.2d 314, 316 (8th Cir. 1993); *Turabo*, 683 F.2d at 26; see also *Resolution Trust Corp. v. Fountain Circle Assocs. Ltd. Partnership*, 799 F.Supp. 48, 50 (N.D.Ohio 1992); *New York Life Ins. Co. v. Watt West Inv. Corp.*, 755 F.Supp. 287, 289-90 (E.D.Cal.1991). Commentators generally approve of the conclusion reached by these courts. *See* 12 Charles Alan Wright et al., Federal Practice and Procedure § 2983, at 33-35 (2d ed.1997); 13 James Wm. Moore et al., Moore's Federal Practice ¶ 66.09 (3d ed.1998).
>
> The conclusion that federal law governs the appointment of receivers is based on several considerations. First and foremost, the appointment of a receiver in equity is not a substantive right; rather, it is an ancillary remedy which does not affect the ultimate outcome of the action. *Pusey & Jones Co. v. Hanssen*, 261 U.S. 491, 497, 43 S.Ct. 454, 456, 67 L.Ed. 763 (1923). The conclusion that federal law governs the appointment of a receiver thus does not conflict with the *Erie* doctrine's requirement that state law apply to matters of substance. *New York Life*, 755 F.Supp. at 291, 12 Wright § 2983, at 34; 13 Moore ¶ 66.09; *see also Skelly Oil Co. v. Phillips Petroleum Co.*, 339 U.S. 667, 674, 70 S.Ct. 876, 880, 94 L.Ed. 1194 (1950) (noting that, in a diversity case, a declaratory remedy may be given by a federal court even if that remedy is unavailable in state court); *Guaranty Trust Co. of New York v. York*, 326 U.S. 99, 65 S.Ct. 1464, 89 L.Ed. 2079 (1945) (stating that the equity power of a federal court exercising diversity jurisdiction cannot be equated with state law under the *Erie* doctrine).
>
> Second, Federal Rule of Civil Procedure 66 and the accompanying Advisory Committee's Note assert the primacy of federal law in the practice of federal receiverships. *New York Life*, 755 F.Supp. at 289-90, 12 Wright § 2983, at 35. Thus, to the extent Rule 66 dictates what principles should be applied to federal receiverships, courts must comply with the Rule even in the face of differing state law. *See Hanna v. Plumer*, 380 U.S. 460, 471, 85 S.Ct. 1136, 1144, 14 L.Ed.2d 8 (1965) (stating that in a diversity case, "[w]hen a situation is covered

> by one of the Federal Rules, ... the court has been instructed to apply the Federal Rule, and can refuse to do so only if the Advisory Committee, this Court, and Congress erred in their prima facie judgment that the Rule in question transgresses neither the terms of the Enabling Act nor constitutional restrictions."); *see also* 12 Wright § 2983, at 34 (stating that the conclusion that federal law governs the appointment of a receiver is consistent with *Hanna*). [footnotes omitted]
>
> *See also, Am. Bank & Trust Co. v. Bond Int'l Ltd.*, No. 06-CV-0317-CVE-FMH, 2006 WL 2385309, at *7 (N.D. Okla. Aug. 17, 2006) (accord).

5. What assets to take must be considered in the Pleadings. The universe is limited to one of two decisions. The decision consists of what needs to be considered is the breath and scope of what needs to be done. Fundamentally, do you take:

a) The assets.

i. These must be defined.

ii. Eliminates confusion.

iii. Is usually faster to convert from a tangible asset(s) to cash, or

b) The entity.

i. Allows for inclusion of things that you do not know at the time of the filing. Sometimes this is good and sometimes it is bad. Knowing the debtor/defendant, their history, their credibility, and their business operations will guide this decision.

ii. More responsibility for dealing with the taxes and other enforcement actions, becomes the responsibility of the Receiver, unless exculpated in the Order Appointing.

c) At the conclusion of the case, the Receivership is dismissed and all of the historical liabilities go back to the debtor/defendant. This is important when there are things like environmental impacts that are not remediated, assets that have a negative value and taxes that cannot be dealt with within the Receivership.

6. Impediments: A Receivership is an extraordinary remedy but at the discretion of the Court, can be invoked. Once a Judge becomes comfortable with the process, they usually will give a great deal of deference to the Receivership process. It allows them to have someone step in and shield the Court from unnecessary work with the best interests of the Court and the parties in mind. The Receiver can make nearly all of the operating decisions,

bring solutions instead of problems to the Court and move a case along, sometimes dragging the parties with them. Below is some support for the appointment:

a) the 5th Circuit Court of Appeals in the case of *Santibanez v. Wier McMahon & Co.*, 105 F.3d 234 (5th Cir. 1997) at page 241 opines:

> Moreover, the District Court had the power to appoint a receiver to take possession of the judgment debtor's property for preservation under Federal Rule of Civil Procedure 66. Under that rule, the appointment of a receiver can be sought "by anyone showing an interest in certain property or a relation to the party in control or ownership thereof such as to justify conservation of the property by a court officer." 7 Moore et al., ¶ 66.05[1]. The appointment is in the sound discretion of the court. *Id*. Similarly, "the form and quantum of evidence required on a motion requesting the appointment of a receiver is a matter of judicial discretion." 12 Charles A. Wright & Arthur R. Miller, Federal Practice and Procedure § 2983 (1973) (citing authorities). Courts have held that receivers may be appointed "to preserve property pending final determination of its distribution in supplementary proceedings in aid of execution." 7 Moore et al., ¶ 66.05 [1] (citing *Haase v. Chapman*, 308 F.Supp. 399 (W.D.Mo.1969)).

b) the 1st Circuit Court Appeals in the case of *Consolidated Rail Corp. v. Fore River Ry. Co.*, 861 F.2d 322 (1st Cir. 1988) beginning at page 326 noted (this is reformatted below to allow for better analysis):

> Courts have recognized many factors that are relevant for a court to consider when determining the appropriateness of the appointment of a receiver. These include:
>
> i. fraudulent conduct on the part of the defendant, *see Burnrite Coal Briquette Co. v. Riggs,* 274 U.S. 208, 212, 47 S.Ct. 578, 579, 71 L.Ed. 1002 (1927);
>
> ii. imminent danger that property will be lost or squandered, *see Gordon v. Washington*, 295 U.S. 30, 37-39, 55 S.Ct. 584, 588-89, 79 L.Ed. 1282 (1935); *Garden Homes, Inc. v. United States*, 200 F.2d 299, 301 (1st Cir.1952);
>
> iii. the inadequacy of available legal remedies, *see Leighton v. One William Street Fund, Inc.*, 343 F.2d 565, 568 (2d Cir.1965);
>
> iv. the probability that harm to the plaintiff by denial of the appointment would be greater than the injury to the parties opposing appointment, *see Mintzer*, 263 F.2d at 825;
>
> v. the plaintiff's probable success in the action and the possibility of irreparable injury to his interests in the property, *see Bookout v. First*

Nat'l Mortgage & Discount Co., 514 F.2d 757, 758 (5th Cir.1975); and

vi. whether the interests of the plaintiff and others sought to be protected will in fact be well served by the receivership, *see Commodity Futures,* 481 F.Supp. at 441.

All of the foregoing do not have to be met, in fact one is sufficient. Additionally, this is not the universe of the reasons that a Receiver should be appointed.

c) the 2nd Circuit Court of Appeals opined in *Citibank, N.A. v. Nyland (CF8) Ltd.*, 839 F.2d 93 (2d Cir. 1988) at page 97:

> We agree with appellants' contention that the appointment of a receiver is not automatic under the mortgage agreement, that "the appointment of a receiver is considered to be an extraordinary remedy", and that the remedy should be employed cautiously and granted only when clearly necessary to protect plaintiff's interests in the property. *Chambers v. Blickle Ford Sales, Inc.*, 313 F.2d 252, 260 (2d Cir.1963). We believe that Citibank made an adequate showing that allowing New York Land to have a continuing role in managing the building would be harmful to the premises' marketability. This harm to its marketability would also reduce the value of the security represented by Citibank's mortgage.
>
> Furthermore, the mortgage agreement between Citibank and Nyland provides that upon the occurrence of any event of default (as explained in the mortgage), Citibank may apply for the appointment of a receiver. Given that it is undisputed that several events of default had occurred, we believe that this provision strongly supports the appointment of a receiver. *See* New York Real Property Law § 254(10); *Meyer v. Indian Hill Farm, Inc.*, 258 F.2d 287, 293-94 (2d Cir.1958); *Febbraro v. Febbraro*, 70 A.D.2d 584, 585, 416 N.Y.S.2d 59 (2d Dep't 1979). It is entirely appropriate for a mortgage holder to seek the appointment of a receiver where the mortgage authorizes such appointment, and the mortgagee has repeatedly defaulted on conditions of the mortgage which constitute one or more events of default. *See, e.g., Mancuso v. Kambourelis*, 72 A.D.2d 636, 637, 421 N.Y.S.2d 130, 131 (3d Dep't 1979); *Febbraro v. Febbraro, supra; Home Title Insurance Co. v. Isaac Scherman Holding Corp.,* 240 A.D. 851, 267 N.Y.S. 84, 85 (2d Dep't 1933). *See also, Am. Bank & Trust Co.,* 2006 WL 2385309, at *7.

7. Power of the Receiver. The Receiver has many of the same powers that a Trustee under 11 USC bankruptcy provisions can invoke. This allows for a case to be handled with efficiency

and mitigates the involvement of the Courts. Again, these are other ways where the Receivership speeds the process along. Some of those powers are:

a) The ability to reject contracts. The Receiver has a right to reject any contracts or leases related to the Assets as found in *Sunflower Oil Co. v. Wilson,* 142 U.S. 313, 322 (1892) and *U.S. Trust Co. v. Wabash W. Ry. Co.*, 150 U.S. 287 (1893).

b) The ability to sell assets free and clear of liens, claims and encumbrances. The limitations are similar to a trustee's, in that they cannot remove deed covenants, avoid certain taxes, and other provisions. It is clear that a Receiver may conduct a sale of assets prior to the entry of a final judgment. One hundred thirty-two (132) years ago, the United States Supreme Court addressed the notion of a Receiver's sale free and clear prior to entry of a final judgment in *First National Bank of Cleveland v. Shedd,* 121 U. S. 74, 7 Sup. Ct. 807, 30 L. Ed. 877 (1887); wherein it was held that there is "no doubt" that a Court has the power to authorize a Receiver to sell property prior to an adjudication of the merits of a foreclosure case.

i. **When defined in the Motion to sell the assets, the sale can force the Right of Redemption or its abandonment.** We include in our sale orders the verbiage that addresses this right by forcing the issue: To protect the Debtor's equity of redemption pursuant to 42 Okl. St. §18, the Sale Order should provide that the Debtor has the right to redeem the property by paying the total amount due on the Creditors' claims in cash at any time prior to the entry of the Confirmation Order. Such procedure protects the Debtor's right to redeem the property by tendering money. The origin of the equity of redemption and the means by which such right is terminated in Oklahoma is the case of *Balduff v. Griswold*, 60 P. 223 (Okla.Terr. 1900), which cites as the origin of such concept the case of *Carr v. Carr*, 52 N.Y. 251 (1873), which in turn cites at page 258 the case of *Murray v. Walker*, 31 N.Y. 399 (1865) wherein at page 404 it was held that a debtor's equity of redemption in mortgaged real property is terminated when they have the "right to answer; and either contest the honesty of the loan, or tender the money and redeem". The Receiver

> requests the Court enter the Sale Order, providing that the equity of redemption afforded to Debtor shall be fully enforceable until entry of the Confirmation Order; and that upon entry of the Confirmation Order, all rights of the Debtor in and to the property including any equity of redemption shall be finally and forever extinguished and that the Receiver's fee is earned in either case.

c) Injunctions to prohibit creditors from gaining a superior position without justification. In nearly every case, creditors attempt to improve their payment position by trying to get a judgement or other priming position to other unsecured creditors. This race to the courthouse can be eliminated by including in the Order Appointing something similar to the following: To facilitate this Court's jurisdiction and to protect the assets in its possession, it has long been held that other parties should not be permitted to interfere with a receiver's administration of the assets held *in custodia legis*. This concept dates back at least 164 years to English common law and the case of *Ames v Birkenhead Dock Trustees* (1855) 20 Beav 332 wherein Lord Romilly, Master of Rolls said "There is no question but that this court will not permit a receiver appointed by its authority, and who is therefore its officer, to be interfered with or dispossessed of the property he is directed to receive, by anyone, although the order appointing him may be perfectly erroneous; this court requires and insists that application should be made to the court, for permission to take possession of any property of which the receiver either has taken or is directed to take possession." Cited with approval by the U. S. Supreme Court in *Barton v. Barbour,* 104 U.S. 126, 129 (U.S. 1881). This Court has authority to issue blanket injunctive relief that is binding on both parties and non-parties as part of this Court's equitable jurisdiction over the assets in this receivership. The recent case of *Liberte Capital Group, LLC v. Capwill*, 462 F.3d 543 (6th Cir. 2006) addressed and specifically approved a blanket injunction binding on both parties and non-parties beginning at page 551:

> Once assets are placed in receivership, a district court's equitable purpose demands that the court be able to exercise control over claims brought against those assets. The receivership court has a valid interest in both the value of the claims themselves and the costs of defending any suit as a drain on receivership assets. *See SEC v. Universal Fin.*, 760 F.2d 1034, 1038 (9th Cir.1985). To this extent,

> the receivership court may issue a blanket injunction, staying litigation against the named receiver and the entities under his control unless leave of that court is first obtained. *See Barton v. Barbour,* 104 U.S. 126, 128, 26 L.Ed. 672 (1881) ("It is a general rule that before suit is brought against a receiver leave of the court by which he was appointed must be obtained.") This power extends to the institution of any suit, and not just a proceeding for execution of a judgment against the receivership in the receivership court. *Id.* at 129, 104 U.S. 126. ("We think, therefore, that it is immaterial whether the suit is brought against [the receiver] to recover specific property or to *552 obtain judgment for a money demand. In either case leave should first be obtained.") Because the court's power of injunction in a receivership proceeding arises from its power over the assets in question, non-parties to the underlying litigation may be bound by a blanket stay, so long as the non-parties have notice of the injunction. *See Bien v. Robinson,* 208 U.S. 423, 427, 28 S.Ct. 379, 52 L.Ed. 556 (1908) (finding "frivolous" the contention that a non-party would not be bound by the court's injunction against claims against a receivership under the court's control); *see also SEC v. Wencke,* 622 F.2d 1363, 1371 (9th Cir.1980) (finding the district court's equitable powers over the property in receivership sufficient to justify a blanket stay against litigation without leave of the court, even against non-parties).
>
> The appointment of a Receiver constitutes an implied injunction against any interference with property in the custody of the Receiver. *See Moller v. Herring,* 255 F. 670, 670 (5th Cir. 1919).

d) Subpoena power can be granted in the Order Appointing Receiver and should be, to facilitate the discovery process. This concept allows the Receiver to find assets and marshal them. It also inspires parties that are reluctant to either divulge or turn over data to do so to avoid being held in contempt of Court or have the Court's protection in the event other parties do not want them to divulge information.

e) If the power to appoint a receiver is included in the loan documents for the Plaintiff creditor, the appointment is nearly guaranteed.

i. *Citibank, N.A. v. Nyland (CF8) Ltd., supra*, because the mortgages provide for the appointment of a Receiver, the application was granted.

f) The ability to bridge operating licenses can be granted in the Order Appointing Receiver. There are times that it is critical for the ongoing operation

of the Receivership Estate business to be able to operate with licenses that are held by the company. This dictates that the Receivership be granted over the entity, not just the assets. Examples:

i. In the healthcare field, without the preservation of the license, the facility has to close and sometimes lose a competitive funding advantage from CMS who pays Medicare and Medicaid. Also, the certificate of need was awarded by the State Department of Health and without it, no new patients or residents can be on-boarded.

ii. In most states where individuals or companies are in the business of selling alcoholic beverages, whether in a package store or in a bar/restaurant, there is a license required to operate. Without the instant preservation of the license, the business closes and the going concern value lost.

g) The assets can be marshalled immediately. The Order Appointing Receiver should include provisions where anyone who is currently holding any assets of any kind (or the proceeds of the sale of the assets) should turn them over to the Receiver and those assets will become a part of the Receivership Estate. The Receiver can analyze the assets and then choose to keep them or reject them, based upon the business judgment rule.

h) Assets of the Receivership Estate are held in Custodia Legis. Once a Receiver is appointed, all property in the possession of the debtor passes into the custody of the Receivership court, and becomes subject to its authority and control. In the exercise of its jurisdiction over the debtor's property, the court has power to issue injunctions and all other writs necessary to protect the estate from interference and to ensure its orderly administration. *Eller Indus., Inc. v. Indian Motorcycle Mfg., Inc.*, 929 F. Supp. 369, 372 (D. Colo. 1995).

8. Forced cooperation by Defendant/Debtors.

i. We include in the Order Appointing Receiver the following paragraph: In the event that any parties to this action or any entities owned by the Defendants, either individually or collectively, have assets in their possession or have transferred assets that may be or was property of the Estate, the parties shall identify those

assets and at the Receiver's discretion, turn the assets over to the Receiver for further disposition. All such property shall be included in the Estate.

9. Forced cooperation by creditors (including injunctive relief).

i. We put in our Orders Appointing Receiver the following paragraph: In order to promote judicial efficiency, all persons who receive actual or constructive notice of this Order are enjoined in any way from disturbing or in any way interfering with the Receiver's administration of the Estate or from prosecuting any new proceedings (including collection or enforcement proceedings) that involve the Receiver or the Estate unless such person or persons first obtain the permission of this Court or the Receiver. All parties to this case and any other entity given notice of this order are hereby enjoined from any and all of the following:

a) the commencement or continuation, including the issuance or employment of process, of a judicial, administrative, or other action or proceeding against the Assets, the Estate or the Receiver that was or could have been commenced before the entry of this Order or to recover a claim against the Assets, the Estate or the Receiver that arose before the entry of this Order;

b) any act to obtain possession of or to exercise control over the Estate or any property thereof;

c) any act to create, perfect, or enforce any lien against the Estate or any property thereof;

d) any act to create, perfect, or enforce against the Estate or any property thereof any lien to the extent that such lien secures a claim that arose before the entry of this Order;

e) any act to collect, assess, or recover a claim against the Assets, the Estate or any property thereof, or the Receiver, that arose before the entry of this Order; or

f) the setoff of any debt related to the Assets that arose before the entry of this Order against any claim against the Assets, the Estate or any property thereof or the Receiver.

10. Forced cooperation by outsiders. We put the following paragraph in the Order Appointing Receiver: **The parties and all other persons or entities served with a copy of this order shall cooperate fully with and assist the Receiver in the performance of his duties** subject to a party's appropriate assertion of the Fifth Amendment privilege against self-incrimination, and other appropriate assertion of any other privilege or right. This cooperation and assistance shall include, but not be limited to, the turnover of any and all Assets, providing any information to the Receiver that the Receiver deems necessary to exercising the authority and discharging the responsibilities of the Receiver under this order; providing any password required to access any computer or electronic files in any medium; turning over any assets (cash or other tangible assets); and advising all persons who owe money to Defendants resulting from Defendants' ownership of the Assets that all such debts should be paid directly to the Receiver.

11. The ability to put the entity into either a Chapter 7 or 11 if circumstances warrant. There are instances that the ability to invoke the powers of the Receivership in other jurisdictions are cumbersome and it is more efficient to use the bankruptcy court to facilitate the process.

12. The ability to issue Receiver's Certificates (Court approved loans). There is the ability, with the Court's approval, where a Receiver can borrow money for the operation of the assets that becomes a super priority obligation and a priming lien similar to § 364 of the Federal Bankruptcy Code.

13. Cost. It is my experience that the cost is substantially less in state court receiverships. The elimination of many of the procedural processes, the types of pleadings, the flexibility of the Receiver versus the trustee or the Debtor in Possession saves money. The lack of mandatory reporting such as the voluminous Monthly Operating Reports saves manpower, which equates to money. The reporting is done on a request basis, typically. The elimination of the first day motions and orders and other basic pleadings also saves time and money. When it comes to a plan, in Receiverships it is done with the sale to a third party or back to the original equity holders and there are no disclosure statements or formal plans, just the sale motions and orders, which are substantially shorter, but still inclusive.

14. Speed.

a) Sales can be done and closed in 75 days.

b) Discovery can be accelerated.

c) Usually the dockets are processed faster.

15. Similar result as a foreclosure, just faster.

a) Free and Clear.

b) With notice and opportunity, the buyer can be in title inside of 75 days.

c) Insurable title.

16. Avoidance of environmental liability for the Plaintiff.

a) One of the biggest fears from a Plaintiff's standpoint is that they could become a 'responsible party' for liabilities that are discovered in the future and that is eliminated because they do not take the asset in title.

b) The Receiver can do the clean-up without incurring any liability. Another utilization of the Judicial Immunity protection awarded to the Receiver.

17. Multi-state jurisdiction is possible by domesticating the case. This can be done by:

a) Filing a separate action in the affected state.

i. This is a short pleading and only deals with the specific assets that need attention in that jurisdiction.

ii. Requesting that the new court take judicial notice of the base case with an emphasis on what is being requested in the new jurisdiction.

18. Operation of a business is flexible.

a) Initially it is better to leave the existing folks in place to maintain continuity. Most of the staff people need and want their jobs and the upper management is not important to the day-to-day operations.

b) However, replace whomever (including the owners) if they cannot be trusted.

19. Tasks that should be granted in the Order Appointing Receiver:

a) Forensic Accounting to determine where the money went.

b) GAAP conversion of the existing accounting to allow all stakeholders to be able to compare the business to some level of standards that would be more easily

defined. Caution is warranted if the historical accounting was done consistently on a tax basis.

c) Valuation of the business or the assets. This is not typically as detailed as an appraisal and is much less costly.

d) Going Concern Analysis should be done superficially in the early stages and then in more depth once the case has progressed and the Receiver has a better handle on the business.

20. Fees and expenses are a super priority and there is a specific lien issued at appointment that extends beyond the life of the case. Without this provision, it is suspect that anyone would want to be appointed. It is important for a Receiver to do a superficial analysis of the assets to determine if they are going to get paid. There are circumstances where one takes a Receivership to assist the Court or the citizens of the community. Those should be considered carefully.

21. Privileged communications. The Receiver can have a provision in the Order Appointing Receiver that allows them privileged communications with all lawyers in the case and their staff. This inclusion usually improves the potential for settlement, since all parties can tell the Receiver the truth and not just the specific side's wants and desires.

22. Corporate Governance. The ability to remove the board of directors and appoint someone else or himself can be done if the Receiver is appointed over the entity. This eliminates the capacity for the Defendant to attempt to put the entity into a Chapter proceeding or do other things that will throw a wrench in the gears of the operation of the business.

23. Acceptance usually requires an education.

a) Many Judges do not understand the process and the scope, so it is important to give the Court enough ammunition to be able to grant the request for the appointment. Once they have appointed a Receiver and it goes smoothly, the subsequent requests are much easier.

b) Many lawyers don't understand how a Receivership benefits their client and their case. On the other hand, the defendant/debtor that does understand will resist, because their client does not want to be exposed to the light of day that the Receivership invokes.

24. A question that has come up and I have not done appropriate research to deal with is: Can a Receiver create a procedure that would allow for the cram down of secured creditors similar to USC §1129 of the bankruptcy code? The answer appears to be NO.

The powers and opportunities of a Receivership can be used by insolvency professionals to benefit their clients and the Courts. This saves time and money for both the Courts and the creditors. Hopefully, the foregoing provides some support for you to use when appropriate.

12 Oklahoma Statutes

A receiver may be appointed by a Judge of the Supreme Court or a district court judge:

1551. In an action by a vendor to vacate a fraudulent purchase of property, or by a creditor to subject any property or fund to his claim, or between partners or others jointly owning or interested in any property or fund, on the application of the plaintiff, or of any party whose right to or interest in the property or fund, or the proceeds thereof, is probable, and where it is shown that the property or fund is in danger of being lost, removed or materially injured.

1552. In an action by a mortgagee for the foreclosure of his mortgage and sale of the mortgaged property or in connection with a mortgagee foreclosing his mortgage by power of sale under the Oklahoma Power of Sale Mortgage Foreclosure Act:

a. where it appears that the mortgaged property is in danger of being lost, removed or materially injured, or

b. that a condition of the mortgage has not been performed, and that the property is probably insufficient to discharge the mortgage debt, or

c. that a condition of the mortgage has not been performed and the mortgage instrument provides for the appointment of a receiver.

1553. After judgment, to carry the judgment into effect.

1554. After judgment, to dispose of the property according to the judgment, or to preserve it during the pendency of an appeal, or in proceeding in aid of execution, when an execution has been returned unsatisfied, or when the judgment debtor refuses to apply his property in satisfaction of the judgment.

1555. In the cases provided in this Code, and by special statutes, when a corporation has been dissolved, or is insolvent, or in imminent danger of insolvency, or has forfeited its corporate rights.

1556. In all other cases where receivers have heretofore been appointed by the usages of the courts of equity.

EXHIBIT A

V. Special Masters

A. John Young

[Special Masters section follows. (257 pages)]

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Special Masters in Bankruptcy: The Case against Bankruptcy Rule 9031

Paulette J. Delk

Special Masters in Bankruptcy: The Case Against Bankruptcy Rule 9031

*Paulette J. Delk**

I. INTRODUCTION

Although American bankruptcy courts hear hundreds of individual, partnership, and corporate bankruptcy cases every year involving complex environmental, tax, tort, and contract issues, bankruptcy courts and the parties before them may not benefit from the assistance of special masters. Rule 9031 of the Federal Rules of Bankruptcy Procedure[1] makes Rule 53 of the Federal Rules of Civil Procedure ("FRCP")[2] governing the appointment and duties of the special master inapplicable in bankruptcy cases. While many courts and commentators recognize that federal courts have inherent authority to appoint special masters,[3] bankruptcy courts have not relied upon this inherent power freely in light of Rule 9031, which could be construed as so restricting the bankruptcy court's authority to appoint special masters as to foreclose the possibility of relying on any other power completely. In this Article, the Author attempts to demonstrate that bankruptcy courts regularly hear cases in which the court and the parties could benefit from the services of a special master and that bankruptcy courts are hampered in their ability to handle cases in the most just and efficient manner possible because of their inability to appoint special masters. Part II of this Article examines the role of the special master in the federal courts generally. It examines the scope of tasks traditionally performed by special masters, as well as the expanded role that special masters have played in recent years as the courts increasingly have relied on special masters in case management. Part III examines the nature of complex bankruptcy cases and the role that special masters could play in these cases. Part IV provides background

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1. FED. R. BANKR. P. 9031; *see infra* note 56 and accompanying text.

2. FED. R. CIV. P. 53.

3. *See, e.g.*, Veneri v. Draper, 22 F.2d 33, 35 (4th Cir. 1927); United States v. Conservation Chem. Co., 106 F.R.D. 210, 217-21 (W.D. Mo. 1985); Jordan v. Wolke, 75 F.R.D. 696, 700-01 (E.D. Wis. 1977); Wayne D. Brazil, *Special Masters in Complex Cases: Extending the Judiciary or Reshaping Adjudication?*, 53 U. CHI. L. REV. 394, 415 n.80 (1986) [hereinafter Brazil, *Special Masters*]; Margaret G. Farrell, *Coping with Scientific Evidence: The Use of Special Masters*, 43 EMORY L.J. 927, 943 (1994) [hereinafter Farrell, *Coping with Scientific Evidence*]; I.H. Jacob, *The Inherent Jurisdiction of the Court*, 23 CURRENT LEGAL PROBS. 23, 34 (1970); *see infra* notes 131-43 and accompanying text.

on the history and rationale for Rule 9031. Part V explores the roles of the examiner and trustee in bankruptcy, and compares those roles with the role of the special master. Part VI discusses the concept of the federal courts' inherent authority to appoint persons to assist the court in performing specific, well-delineated judicial tasks in furtherance of the efficient administration of cases.

II. SPECIAL MASTERS IN FEDERAL COURTS GENERALLY

A. A Brief History

The practice of appointing special masters to provide assistance to courts is a long and well-established one. Some historians believe that the practice of appointing persons to assist the court, through a formal process, was first established in early Roman law through the use of the judex—a private person appointed by a praetor, with the consent of the parties to an action, to hear and decide the case.[4] Special masters were used in England at least as far back as the seventeenth century (introduced in the British legal system by the Normans, some historians believe), although the actual benefit to the court, and, especially to the parties, was questionable at that time.[5] The practice of appointing special masters to assist the court continued in America beginning at least as early as the eighteenth century.[6] Not long thereafter, the federal judiciary began to use

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4. *See* 1 DAN B. DOBBS, LAW OF REMEDIES § 2.8(1), at 190 (2d ed. 1993); 1 WILLIAM S. HOLDSWORTH, A HISTORY OF ENGLISH LAW 416 (A. Goodhart & H. Hanbury eds., 7th ed. rev. 1956); 1 FREDERICK POLLOCK & FREDERIC W. MAITLAND, HISTORY OF ENGLISH LAW 193 (1959); 2 CHARLES P. SHERMAN, ROMAN LAW IN THE MODERN WORLD §§ 849, 881, at 404, 434 (1937); James R. Bryant, *The Office of Master in Chancery: Early English Development*, 40 A.B.A. J. 498, 498 (1954); *see also* Simpson v. Canales, 806 S.W.2d 802, 806-11 (Tex. 1991) (reviewing the history of special masters).

5. *See generally* 1 HOLDSWORTH, *supra* note 4, at 424-25 (describing generally the abuses in the system); Irving R. Kaufman, *Masters in the Federal Courts: Rule 53*, 58 COLUM. L. REV. 452, 452 (1958) (citing 6 THE WORKS OF JEREMY BENTHAM 43 (Bowring ed., 1843); 9 WILLIAM S. HOLDSWORTH, A HISTORY OF ENGLISH LAW 360 (3d ed. 1944) (describing the masters' practice of delaying proceedings for the purpose of charging a special fee for acceleration, and increasing the number of appearances before the master and the number of services that the masters were required to perform to increase fees); Linda J. Silberman, *Masters and Magistrates Part I: The English Model*, 50 N.Y.U. L. REV. 1070, 1075-79 (1975) (describing the history of the special master system in England)).

6. *See* James R. Bryant, *The Office of Master in Chancery: Colonial Development*, 40 A.B.A. J. 595, 598 (1954) (describing the history and process of development of the special master in colonial America); Linda J. Silberman, *Masters and Magistrates Part II: The American Analog*, 50 N.Y.U. L. REV. 1297, 1321-22 (1975) (noting that special

special masters on a regular basis to handle discrete aspects of cases, such as taking and reporting testimony,[7] determining questions at issue where facts and evidence were complex and voluminous,[8] and auditing and stating accounts.[9] Early on, federal courts held that they had the authority to appoint special masters through their "inherent power to provide themselves with appropriate instruments required for the performance of their duties."[10] Courts pointed to this inherent power as their authority to appoint special masters even over the objections of the parties.[11] Many courts held, however, that this inherent power was bound by limitations imposed through Article III of the United States Constitution[12] and determined that it was inappropriate to refer to the special master matters that were determinative of a "fundamental issue of liability" because the special masters do not meet the requirements imposed by Article III.[13] As a result, in the absence of the full consent of all of the parties, the most widely accepted practice was to refer matters to the special master that were narrow, well-defined, and specific.[14]

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masters have been a part of the federal judiciary of the United States since its inception).

7. *See, e.g.*, Holt Mfg. Co. v. C.L. Best Gas Traction Co., 245 F. 354, 357 (N.D. Cal. 1917).

8. *See, e.g.*, United States *ex rel.* Brading-Marshall Lumber Co. v. Wells, 203 F. 146, 148-49 (E.D. Tenn. 1913).

9. *See, e.g.*, Thompson v. Smith, 23 F. Cas. 1092 (C.C. Ohio 1869).

10. *In re* Peterson, 253 U.S. 300, 312 (1920); *see also supra* notes 131-43 and accompanying text.

11. *Peterson*, 253 U.S. at 312. According to the *Peterson* court:

> This power includes authority to appoint persons unconnected with the court to aid judges in the performance of specific judicial duties, as they may arise in the progress of a cause. From the commencement of our government it has been exercised by the federal courts, when sitting in equity, by appointing, either with or without the consent of the parties, special masters. . . .

Id.

12. U.S. CONST. art. III, § 1:

> The judicial Power of the United States, shall be vested in one supreme Court, and in such inferior Courts as the Congress may from time to time ordain and establish. The Judges, both of the supreme and inferior Courts, shall hold their Offices during good Behaviour, and shall, at stated Times, receive for their Services, a Compensation, which shall not be diminished during their Continuance in Office.

13. *See* Stauble v. Warrob, 977 F.2d 690, 695-96 (1st Cir. 1992) (citing *In re* Bituminous Coal Operators' Ass'n, 949 F.2d 1165, 1168 (D.C. Cir. 1991); Burlington N. R.R. v. Dep't of Revenue, 934 F.2d 1064, 1073 (9th Cir. 1991)). The attributes most commonly cited are lifetime tenure and the protection from the diminution of salary.

14. Where the parties have not consented, the courts traditionally treat the special master's report as advisory, to be adopted by the court only to the extent that the court agrees with it after making an independent review of the entire record. *See, e.g.*, Heckers

B. Current Use of Special Masters

As a part of the 1938 enactment of the FRCP, Rule 53(b) specifically authorized the appointment of special masters.[15] FRCP 53(b) was drafted to follow the basic practices and guidelines of the earlier Equity Rules[16] and to clarify certain of those practices. Like the Equity Rules, FRCP 53(b) contemplates specific and well-defined duties for the special master in the federal court system. Although some courts have expanded the role of the special master in a manner that has generated some controversy[17] and have justified the appointment of special masters for controversial reasons,[18] there remain some clear-cut and uncontroversial roles for special masters. These roles involve duties, such as accounting and computation, determining relevant issues under circumstances where the evidence is voluminous,[19] and advising the court on severable issues that are highly technical in nature.[20] The appointment of special masters to perform these duties is seldom questioned by the parties, courts, or commentators. These tasks and duties assigned to and performed by special masters are generally held to be invaluable aids to the federal courts. In complex litigation, where there are often hundreds, and sometimes thousands,

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v. Fowler, 69 U.S. (2 Wall.) 123, 131-33 (1864); Mastin v. Noble, 157 F. 506, 508 (8th Cir. 1907); Holt Mfg. Co. v. C.L. Best Gas Traction Co., 245 F. 354, 356 (N.D. Cal. 1917); *In re* Thomas, 45 F. 784, 787 (D.C.S.C. 1891).

15. FED. R. CIV. P. 53(b).

16. Rules of Practice for the Courts of Equity of the United States, 42 U.S. (1 How.) xli-lxx (1842).

17. The use of special masters in pretrial management has been questioned by many as an improper expansion of the traditional use of special masters because it requires the exercise of judicial authority, which special masters do not have. *See, e.g.*, MANUAL FOR COMPLEX LITIGATION § 20.14, at 16 (3d ed. 1982); Wayne D. Brazil, *Referring Discovery Tasks to Special Masters: Is Rule 53 a Source of Authority and Restrictions?*, 1 AM. B. FOUND. RES. J. 143, 143-44 (1983) [hereinafter Brazil, *Referring Discovery Tasks*] (The author found that, although Rule 53 may not authorize the use of special masters to perform pretrial management matters, courts still may appoint special masters to perform these duties through their inherent authority.).

18. *See* LaBuy v. Howard Leather Co., 352 U.S. 249, 251-55 (1957). In *LaBuy*, the Supreme Court indicated that under Rule 53, calendar congestion, complexity of the issues, and the possibility of a lengthy trial were insufficient reasons to appoint a special master whose duties were to carry out the full fact-finding function on the merits of the case. *Id.* at 259. The Court determined that the use of the master in this manner displaced the court rather than aiding it. *Id.*

19. *See In re* Peterson, 253 U.S. 300, 312 (1920).

20. *See* Danville Tobacco Ass'n v. Bryant-Buckner Ass'n, 333 F.2d 202, 208-09 (4th Cir. 1964) (where a district court appointed an official in a tobacco association to assist it in making judgments regarding tobacco marketing, a highly technical market).

of claims in a single case, special masters have been assigned to assist the court in performing a variety of discrete functions.[21] In complex cases, district court judges often appoint special masters to summarize and evaluate claims, and to develop and implement case management and evaluation plans.[22] Two frequently cited, complex cases in which special masters were appointed to evaluate claims and develop case management plans are the Alabama DDT case[23] and the Ohio asbestos case.[24] In these cases, the special masters are credited with developing innovative plans and data collection systems that greatly aided the courts in streamlining the cases and bringing about their resolution.[25] The Alabama DDT and Ohio asbestos cases involved an extraordinary amount of evidence and claims, and, for that reason, may be viewed as unusual cases. But there are other complex litigation cases, without the extraordinary volumes of evidence and claims found in the Alabama DDT and the Ohio asbestos cases, in which special masters have been used quite effectively. Special masters were appointed, in these more commonplace cases,

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21. For a thorough analysis of the use of special masters in complex litigation, see Brazil, *Special Masters*, *supra* note 3, at 394. *See also* Francis E. McGovern, *Toward a Functional Approach for Managing Complex Litigation*, 53 U. CHI. L. REV. 440, 478-91 (1986) (noting that special masters are used often in complex litigation to provide expert, technical assistance, but, just as frequently, they are used to provide advice on techniques for gathering and analyzing large amounts of empirical data).

22. To the extent that the special master's assigned duties include discovery responsibilities, some have questioned the district court's authority under Rule 53 to make such assignments to special masters. *See generally* Brazil, *Special Masters*, *supra* note 3, at 395-98. Nevertheless, special masters are frequently appointed to supervise discovery in complex cases. *See, e.g.*, Nat'l Ass'n of Radiation Survivors v. Turnage, 115 F.R.D. 543, 558 (N.D. Cal. 1987) (special master appointed to resolve discovery disputes where egregious discovery disputes found to exist); United States v. Conservation Chem. Co., 106 F.R.D. 210, 214 (W.D. Mo. 1985) (affirming the appointment of a special master in a case involving voluminous technical and scientific data); *In re* Agent Orange Prod. Liab. Litig., 94 F.R.D. 173, 173-75 (E.D.N.Y. 1982) (affirming the appointment of a special master in a case involving more than four million documents); United States v. Int'l Bus. Machs. Corp., 76 F.R.D. 97, 98-99 (S.D.N.Y. 1977); Fisher v. Harris, Upham & Co., 61 F.R.D. 447, 449-53 (E.D.N.Y. 1973).

23. Wilhoite v. Olin Corp., No. CV-83-C-5021-NE (N.D. Ala. filed 1983); Hagood v. Olin Corp., No. CV-83-C-5917-NE (N.D. Ala. filed 1983).

24. *In re* Related Asbestos Cases (N.D. Ohio filed 1983).

25. *See, e.g.*, Jerome I. Braun, *Special Masters in Federal Court*, 161 F.R.D. 211, 215-20 (1995); Margaret G. Farrell, *The Role of Special Masters in Federal Litigation*, C842 ALI-ABA 931, 946-51 (1993) [hereinafter Farrell, *Role of Special Masters*]; Jonathan S. Liebowitz, *Special Masters: An Alternative Within the Court System*, 48 DISP. RESOL. J. 64, 66-67 (1993).

to supervise discovery depositions, evaluate services, conduct surveys, receive confidential and privileged documents, and review highly technical documents.[26]

In recent years, judges and lawyers have given increased attention to active judicial case management, including devices such as: pretrial scheduling, and settlement conferences; discovery limits and deadlines; innovative methods of hearing and disposing of motions; and case monitoring. Judicial intervention through these case management devices reduces both the duration and expense of litigation. Costs are reduced when judicial management causes settlement of a case at an earlier stage of the process—thus eliminating the transaction costs of motions and discovery that otherwise might have occurred. Costs and duration are also reduced when pretrial conferences succeed in refining issues, which, in turn, may reduce the number and extent of motions and discovery.[27]

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26. *See, e.g., In re* U.S. Dep't of Def., 848 F.2d 232, 235-37 (D.C. Cir. 1988) (special master appointed to review sensitive government documents because the special master already had security clearance and was an intelligence expert with the ability to develop a sample of the documents and to summarize the reasonable positions that the parties might take on the possible exemption of each document); *In re* Armco, Inc., 770 F.2d 103, 105 (8th Cir. 1985) (affirming the district court's appointment of the special master to supervise and conduct pretrial matters, including discovery activity, the production and arrangement of exhibits and stipulations of fact, and the power to hear motions for summary judgment or dismissal); First Iowa Hydro Elec. Co-op. v. Iowa-Illinois Gas & Elec. Co., 245 F.2d 613, 628 (8th Cir. 1957) (special masters appointed to take discovery depositions that the court felt needed continuous supervision, and externally imposed an order that a master could provide), *cert. denied*, 355 U.S. 871 (1957); Costello v. Wainwright, 387 F. Supp. 324, 327-28 (M.D. Fla. 1973) (In this class action suit brought by Florida prisoners alleging constitutional deprivations caused by inadequate health care provided in the prison system, the court appointed a special master to aid the court in evaluating the quality of medical services provided to the inmates. The special master assisted the court by "organizing, directing and conducting a comprehensive survey of the health care services provided by the Florida Division of Corrections to inmates committed to its custody, and to report his findings to the Court."); TransAmerican Natural Gas Corp. v. Mancias, 877 S.W.2d 840, 843 (Tex. App. 1994) (The appellate court affirmed a district court's appointment of a special master to receive discovery documents that opposing counsel alleged to be confidential and privileged by ruling that it was proper for the court to appoint a special master with special training to assist in reviewing documents of such a technical nature to determine questions of privilege and discoverability.); *see also* United States v. Conservation Chem. Co., 106 F.R.D. 210, 216 (W.D. Mo. 1985); *In re* Agent Orange Prod. Liab. Litig., 94 F.R.D. 173, 174 (E.D.N.Y. 1982).

27. *See generally* Jaquette v. Black Hawk County, Iowa, 710 F.2d 455, 463 (8th Cir. 1983); MAUREEN SOLOMON & DOUGLAS SOMERLOT, TASK FORCE ON REDUCTION OF LITIG. COST AND DELAY, JUD. ADMIN. DIVISION, A.B.A., CASEFLOW MANAGEMENT IN THE TRIAL COURT (1987); MAUREEN SOLOMON & DOUGLAS SOMERLOT, LAW. CONF. TASK FORCE ON REDUCTION OF LITIG. COST AND DELAY, A.B.A., DEFEATING DELAY: DEVELOPING AND IMPLEMENTING A COURT DELAY REDUCTION PROGRAM (1986); Terry

Special masters have come to represent an important element in the use of these case management devices and in the overall search for ways of bringing cases to a just and acceptable end as quickly as possible.[28] Special masters have been important to the courts, particularly in settlement discussions, because of the more informal nature of the role of the special master.[29] Courts also have begun to appoint special masters with increasing frequency at the pretrial stage to facilitate settlements by delegating some tasks to the special master to minimize direct judicial involvement in settlement efforts early on and to avoid the appearance of bias or prejudgment.[30] Effective and efficient case management requires flexibility.[31] Lawyers and judges have come to accept that

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Hackett, *California Adopts New Case Management Rules to Reduce Delay*, 75 JUDICATURE 108 (1991); Maureen Solomon & Holly Bakke, *Case Differentiation: An Approach to Individualized Case Management*, 73 JUDICATURE 17 (1989); Hubert L. Will, *Judicial Responsibility for the Disposition of Litigation*, 75 F.R.D. 117, 125 (1978).

28. *See generally* Liebowitz, *supra* note 25 (describing how special masters can assist the courts in controlling the length of complex litigation). Federal courts also are increasingly turning to court-appointed managerial experts for assistance. For a thorough discussion of the courts' use of these experts and their authority to appoint them, see generally Ellen E. Deason, *Managing the Managerial Expert*, 1998 U. ILL. L. REV. 341.

29. *See, e.g.*, Jerome I. Braun, *Special Masters in Federal Court*, 161 F.R.D. 211, 218 (1995) (noting the role of the special master in facilitating settlement discussions, advising the court, and evaluating the claims of parties); Farrell, *Role of Special Masters*, *supra* note 25, at 946-49 (noting the role of the special master in discovery and settlements, and as advisors, fact finders, and case managers); Liebowitz, *supra* note 25, at 65 (reviewing a case in which a special master held eighty-five hearings in which 166 plaintiffs had claims against three defendants and in which the use of the special master had a significant impact on the court's ability to conclude the case at all).

30. Judicial participation in the settlement process is the subject of much debate. While some believe that judges can and should play a major role in helping parties achieve settlement, others believe that the extent and nature of the judge's role in settlement matters should be limited so that the judge can maintain neutrality and can render a disinterested opinion should settlement discussions fail. *See, e.g.*, DORIS MARIE PROVINE, SETTLEMENT STRATEGIES FOR FEDERAL DISTRICT JUDGES 23 (1986) (discussing disagreement among trial judges as to the proper involvement of the judiciary in the use of particular settlement techniques); E. Donald Elliott, *Managerial Judging and the Evolution of Procedure*, 53 U. CHI. L. REV. 306, 322-23 (1986) (reviewing and discussing the change in emphasis from narrowing issues in the pretrial phase to promoting settlement).

31. Increasingly, courts have found a variety of innovative ways in which special masters can assist the court. *See, e.g.*, *In re* Joint E. & S. Dist. Asbestos Litig., 129 F.R.D. 434, 435 (E.D.N.Y. & S.D.N.Y. 1990) (special master appointed expressly to achieve settlement of this complex case); *In re* Agent Orange Prod. Liab. Litig., 94 F.R.D. 173, 173-75 (E.D.N.Y. 1982) (The use of a special master to supervise discovery and prepare the pretrial order was justified in light of the "sheer volume of documents to be reviewed, the number of witnesses to be deposed, [and] the need for a speedy

differences in complexity and subject matter of lawsuits present the need for different types of case management practices. The appointment of special masters is one of the case management practices frequently employed by the courts because it has proven to be particularly effective and efficient.

III. POTENTIAL USE OF SPECIAL MASTERS IN BANKRUPTCY CASES

In bankruptcy cases requiring the estimation of claims, computation of damages, valuation hearings, and, in cases of corporate debtors, highly technical companies, the appointment of a special master could prove to be particularly beneficial to the bankruptcy court. Often, a large, complex, corporate Chapter 11[32] case with numerous claimants[33] requires estimation of claims, computation of damages, and valuation hearings. The bankruptcy court is required to estimate any unliquidated or contingent claim, the "fixing or liquidation of which . . . would unduly delay the closing of the case."[34] Where there are numerous claims of this type, a special master could be appointed by the bankruptcy court to review the potential claims and to develop a method or propose a formula for estimating the claims in question.[35] Particularly in cases where the debtors are

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processing of all discovery problems in order to meet the trial date"); Costello v. Wainwright, 387 F. Supp. 324, 325-26 (D.C. Fla. 1973) (special master appointed to evaluate the quality of medical services).

32. 11 U.S.C. §§ 1101-1174 (2000). Chapter 11 is primarily designed for the reorganization of the debts of a business through a reorganization plan. The plan must be voted upon by specified creditors and shareholders, and must be confirmed by the court.

33. Corporations and sole proprietorships filed 9,947 Chapter 11 cases in the twelve-month period ending June 30, 2000. *See Filings*, Bankr. L. Daily (BNA) (Aug. 15, 2000) (reporting based on data released by the Administrative Office of the United States Courts); *see also* Alexander D. Bono, *Class Action Proofs of Claim in Bankruptcy*, 96 COM. L.J. 297, 297 (1991) (noting the rise in class action issues arising in bankruptcy cases).

34. 11 U.S.C. § 502(c) (2000). For examples of situations in which the courts have estimated claims in a Chapter 11 context, see *In re Thomson McKinnon Securities, Inc.*, 191 B.R. 976, 979-81 (Bankr. S.D.N.Y. 1996) (estimation of claims involving trust accounts and churning claims against the debtor); *Beatrice Co. v. Rusty Jones, Inc.*, 153 B.R. 535, 536-37 (N.D. Ill. 1993) (estimation of contingent claims and validation of liquidated claims in a Chapter 11 case).

35. At least one commentator has suggested that special masters could be helpful to a bankruptcy court "when it must estimate the values of a large number of claims in which the debtor has admitted liability. In these situations, special masters may obviate the need for any oral hearing, [because] valuation of damages often involves more concrete, objective factors than does evaluating liability." David Kauffman, *Procedures for Estimating Contingent or Unliquidated Claims in Bankruptcy*, 35 STAN. L. REV. 153, 170 (1982) (internal citations omitted).

involved in highly technical areas, the appointment of a special master with specific expertise could prove to be an invaluable service to the court and could expedite matters considerably.

In *In re White Motor Credit Corp.*,[36] the bankruptcy court, presiding over a Chapter 11 case involving a corporation and five of its affiliates in which there were 160 products liability suits pending in state and federal courts across the country, with the potential for the existence of many more unfiled suits, proposed the appointment of a special master for just that purpose.[37] The court proposed appointing the special master to assist it in developing a program for resolving the 160 pending product liability cases and for identifying and resolving the potential unfiled product liability cases, and to "conduct hearings on non-settled claims."[38] The court cited as reasons for the use of the special master: (1) the amount of time that it was already spending on this case on a daily basis; (2) the fact that travel to the residences of the parties and the witnesses may be required; and (3) the inappropriate use of the court's time in addressing what would be "'matters of account and . . . difficult computation of damages.'"[39] These are the same reasons why district courts appoint special masters, and they are the same tasks that special masters appointed by the district courts perform.[40] Ultimately, the bankruptcy court was unable to appoint a special master in this case—not because the services of a special master were not warranted—but due to jurisdictional issues.[41]

The only case in which a bankruptcy court successfully appointed a special master is a case in a Puerto Rican bankruptcy court, which involved the reorganization of a broadcasting company.[42] Upon the petition of the creditors' committee, the bankruptcy court appointed a special master for the express purpose of negotiating and conducting the sale of two television stations.[43] The

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36. 11 B.R. 294 (Bankr. N.D. Ohio 1981).

37. *See id.* at 296. The appointment of a special master to assist in the formulation of a program to determine and resolve product liability claims was approved in this case, but, on appeal, the court determined that the state courts where cases were initially pending were the proper forums for resolving these cases and not the bankruptcy court. *In re* White Motor Credit, 761 F.2d 270, 275 (6th Cir. 1985). The state courts were deemed to be the proper forums because there were some defendants in the tort cases who could not be transferred out of the jurisdiction, meaning that the cases would "have to be tried twice in different courts" if the federal court heard some of the cases. *Id.* at 273-74. Thus, in the interest of justice and judicial economy, and because state issues predominated, these cases remained in the state courts and were tried by state judges.

38. *In re White*, 11 B.R. at 295.

39. *Id.* at 297 (quoting FED. R. CIV. P. 53(b)).

40. *See supra* notes 22-26 and accompanying text.

41. *In re White*, 761 F.2d at 271.

42. *In re* Am. Colonial Broad. Corp., 758 F.2d 794 (1st Cir. 1985).

43. *Id.* at 796.

sale of this kind of asset requires special knowledge and expertise, and the court saw the need for the assistance of an individual with special knowledge in this area. The court did not give the special master the final decision in this matter; rather, it retained the power to make the final decision regarding whether to allow the sale to go forward, thus maintaining the special master's duty as a specific, discrete one—not one that was case determinative.[44] The order appointing the special master was appealed by the losing bidder, the debtor, but the appeal was unsuccessful because both the district court and the court of appeals held that the order was not a final one—thus, it could not be appealed unless an applicable exception existed (and the court of appeals held that no such exception applied in this case).[45] This case stands alone among reported bankruptcy cases in which a bankruptcy judge appointed a special master and in which the special master actually performed the designated services.

In many districts, the most frequent need for a special master in a bankruptcy case is in the self-employed, small-business Chapter 13 cases[46] in which there is reason to believe that greater assets and income exist than noted in the schedules, but where the debtor's records are in a chaotic state, and require extensive effort to track down and sort through to verify the accuracy of the bankruptcy schedules. This assistance could be very helpful to the creditors and to the court, but it would not be an efficient use of the court's time. The standing Chapter 13 trustees[47] are unable to devote the time that would be required to fulfill this task because of the sheer volume of Chapter 13 cases in many districts.[48] As a result, the potential benefit to creditors, in many of these cases, would merit the appointment of a special master.

In Chapter 11 cases, there are frequent motions to modify the automatic stay[49] in which the court must determine the value of the property at the center of the controversy in order to decide if the automatic stay should be modified.

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44. *See supra* note 14 and accompanying text.

45. *In re Am. Colonial*, 758 F.2d at 798-803.

46. 11 U.S.C. §§ 1301-1330 (2000). This Chapter, as its title suggests, is designed to provide for the "Adjustment of Debts of an Individual with Regular Income." Debtors propose a payment plan generally of a three-to-five-year duration, which must be confirmed by the court, and, in return, the debtors receive a discharge from most remaining debts upon completion of the plan.

47. 11 U.S.C. § 1302(a) (2000); *see also* 28 U.S.C. § 586(b) (1994). These statutes permit the appointment of a person to serve as the trustee in the Chapter 13 cases filed in a particular region when the number filed in the region warrants the full-time attention of a single trustee. Many districts have the services of a standing trustee, and some districts with extremely large Chapter 13 filings have the services of more than one standing trustee.

48. *See Filings*, *supra* note 33 (For the twelve-month period ending June 30, 2000, there were 380,770 Chapter 13 cases filed.).

49. 11 U.S.C. § 362 (2000).

Often, both the creditor and the debtor present appraisals of the property, but the court must reach an independent decision as to the actual value of the property for purposes of deciding whether the creditor's motion to modify the automatic stay should be granted. Also, in Chapter 11 cases, the court must determine whether the plan of reorganization is feasible.[50] Whether the plan is feasible or not depends, in large part, on financial information regarding the debtor and whether the data demonstrate, *inter alia*, that the debtor's capital structure and earning power are adequate to support the plan of reorganization.[51] Creditors who object to the plan of reorganization may present data to dispute the debtor's projections. The court must analyze all of the information in order to make an independent determination regarding the feasibility of the plan of reorganization. In both instances, a special master could provide valuable assistance to the court in analyzing the various appraisals and financial data provided by the debtor and creditors.

Among the multitude of bankruptcy cases filed annually,[52] there are many cases that require specific and easily delineated tasks, such as the estimation of claims,[53] computation of damages, and analysis and assessment of appraisals and

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50. 11 U.S.C. § 1129 (a)(11) (2000).

51. *See, e.g., In re* Merrimack Valley Oil Co., 32 B.R. 485, 488-91 (Bankr. D. Mass. 1983); *In re* Landmark at Plaza Park Ltd., 7 B.R. 653, 658-60 (Bankr. D.N.J. 1980).

52. *See Filings, supra* note 33. In the twelve-month period ending June 30, 2000, there were 1,276,922 bankruptcy petitions filed; in the twelve-month period ending June 30, 1999, 1,352,030 petitions were filed.

53. Under the Bankruptcy Act of 1898, ch. 541, § 57(d), 30 Stat. 544 (repealed 1979), not all claims were required to be estimated. Section 57(d) of the Act provided that if the estimation of a contingent or unliquidated claim would unduly delay the administration of the estate or any proceeding under this Act, the claim would not be allowed. The result was that the creditor's claim would be unaffected by the discharge in bankruptcy, and the creditor could pursue the debtor after the claim was fixed or liquidated despite the debtor's discharge. Section 502(c) of the Code requires the estimation of contingent or unliquidated claims when the fixing or liquidation of those claims would unduly delay the administration of the case. 4 COLLIER ON BANKRUPTCY ¶ 502.04[1], at 502-51 (Lawrence P. King ed., 15th ed. rev. 2001). Congress wanted "to afford the debtor complete bankruptcy relief," and § 502(c) was one means that Congress used to achieve this goal. H.R. REP. NO. 95-595, at 352 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5787, 6308. Section 502(c)'s estimation of the claims requirement adds to the number of claims in which the court directly must involve itself by taking evidence to determine the proper estimation. Where a claim is fixed, liquidated, and well-documented, the claim is automatically allowed without a review by the court, unless a party in interest objects to the claim. 11 U.S.C. § 502(c) (2000).

In the reorganization under Chapter 11 of one chemical company, the potential existed for the individual estimation of 187 contingent and unliquidated claims against the debtor. *In re* Borne Chem. Co., 16 B.R. 509, 512 (Bankr. D.N.J. 1980).

financial data. These kinds of tasks make the appointment of a special master a practical and desirable addition to the tools available to assist the district court and bankruptcy judge in bankruptcy cases. Moreover, these tasks involve the kind of services that masters historically have performed.[54]

IV. SPECIAL MASTERS PROHIBITED IN BANKRUPTCY

A. Source of the Prohibition

Although there are many kinds of proceedings in which a bankruptcy court may benefit from the services of a special master, bankruptcy courts are not authorized to appoint special masters at this time. Because of a bankruptcy rule that expressly prohibits the appointment of a special master in bankruptcy cases, special masters may not be appointed by bankruptcy judges.[55] The Bankruptcy Code provides no statutory prohibition against the appointment of special masters; the only prohibition against the appointment of a special master in bankruptcy cases is set forth in a procedural rule that states: "Masters Not Authorized: Rule 53 F.R.Civ.P. does not apply in cases under the Code."[56]

This procedural rule, Bankruptcy Rule 9031, is a single, simple sentence providing neither guidance nor elucidation.[57] A Committee Note, also a single, simple sentence, follows the rule, stating: "Committee Note: This rule precludes the appointment of masters in cases and proceedings under the Code."[58] The note only adds the word "proceedings" to the word "cases" in its "discussion" of the Bankruptcy Rule that makes FRCP 53 of the FRCP inapplicable under the Code.[59] This single-sentence rule and the lack of a true explanation or discussion in the Committee Note calls into question the authority of even the district court to appoint a special master in a bankruptcy case.[60] The rule is not limited in its application to bankruptcy cases that are before the

54. 1 DOBBS, *supra* note 4, § 6.6(1), at 133 (noting that masters traditionally performed specific tasks associated with taking evidence).

55. FED. R. BANKR. P. 9031.

56. FED. R. BANKR. P. 9031. In contrast, the Bankruptcy Code expressly prohibits bankruptcy judges from appointing receivers in bankruptcy cases. 11 U.S.C. § 105(b) (2000).

57. FED. R. BANKR. P. 9031.

58. FED. R. BANKR. P. 9031.

59. FED. R. BANKR. P. 9031.

60. *See supra* notes 56-58 and accompanying text.

bankruptcy court.[61] Rather, it is apparently applicable to all courts hearing a bankruptcy case, including the district court.[62]

The only other published and official explanation for Rule 9031 comes from the Advisory Committee on Bankruptcy Rules' preface to the then-proposed Rules of Bankruptcy Procedure in which the Committee provided discussion of each of the proposed rules.[63] In its discussion of proposed Rule 9031, the Advisory Committee reviewed former Bankruptcy Rule 513,[64] which made FRCP 53 applicable in bankruptcy cases, and explained: "There does not appear to be any need for the appointment of special masters in bankruptcy cases

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61. FED. R. BANKR. P. 1001 provides: "The Bankruptcy Rules and Forms govern procedure in cases under title 11 of the United States Code. . . . These rules shall be construed to secure the just, speedy, and inexpensive determination of every case and proceeding." Should the United States district court withdraw the reference of a bankruptcy case or proceeding from the bankruptcy court, the district court judge would be prohibited from appointing a special master in the bankruptcy case or proceeding because of Rule 9031, despite the fact that the case or proceeding is one in which the appointment of a special master greatly would assist the court in "secur[ing] the just, speedy, and inexpensive determination of [the] case." *Id.*

62. *See* Jack B. Weinstein, *Some Benefits and Risks of Privatization of Justice Through ADR*, 11 OHIO ST. J. ON DISP. RESOL. 241, 271 ("The propriety of appointing special masters in bankruptcy cases is subject to some dispute. This consideration led the author to use a semantic substitute—the court-appointed 'special advisor'—in the Manville Bankruptcy-Trust litigation." (footnotes omitted)). Mark Peterson, the special advisor to the court in *In re Joint E. & S. Dist. Asbestos Litig.*, 878 F. Supp. 473, 573 (E.D.N.Y. & S.D.N.Y. 1995), *aff'd*, 100 F.3d 944 (2nd Cir. 1996), the case referred to by Judge Weinstein, was appointed to develop a plan for restructuring the trust payment schedule and refinancing the trust, and to evaluate the claims by the type of disease. These are duties traditionally assigned to special masters. *See also* Minerex Erdoel, Inc. v. Sina, Inc., 838 F.2d 781, 783 (5th Cir. 1988), *cert. denied*, 488 U.S. 817 (1988); *In re* Elcona Homes Corp., 810 F.2d 136, 140 (7th Cir.1987) (Both cases support the proposition that district courts may not allow the appointment of a special master in a bankruptcy case through their reference powers.).

63. [A] COLLIER ON BANKRUPTCY app. pt. 2(b), at 2-120 to 2-124 (Lawrence P. King ed., 15th ed. rev. 2001).

64. FED. R. BANKR. P. 513, titled *Special Masters*, provided: "if a reference is made in a bankruptcy case by a judge to a special master, the Federal Rules of Civil Procedure applicable to masters apply." FED. R. BANKR. P. 513 (repealed Aug. 1, 1983), *reprinted in* 12 COLLIER ON BANKRUPTCY, at 5-103 (James Wm. Moore & Lawrence P. King eds., 14th ed. 1978). COLLIER ON BANKRUPTCY explains: "The word 'judge' meant the United States district judge, not the bankruptcy judge." [A] COLLIER ON BANKRUPTCY app. pt. 2(b), at 2-122 (Lawrence P. King ed., 15th ed. rev. 2001). Accordingly, former Rule 513 generally applied only when a Chapter X case was retained by the district judge although it probably would apply when a district judge removed any case from the bankruptcy court to the district court. *See* FED. R. BANKR. P. 102(b) (repealed Aug. 1, 1983).

by bankruptcy judges. The Advisory Committee, therefore, has decided that former Rule 513 not be continued in the rules and that Rule 53 F. R. Civ. P. not be made applicable."[65] The Advisory Committee has given no further explanation for its decision that there no longer would be a need for the appointment of special masters in bankruptcy cases.[66] Given the language of Rule 9031,[67] making FRCP 53 inapplicable in all bankruptcy cases, no judge, whether of the district court or bankruptcy court, is authorized to appoint a special master. This kind of prohibition did not extend to district court judges under the Bankruptcy Act.[68] It is difficult to believe that this was the intended result of the rule, but it is the necessary result when the clear and unambiguous language of the rule is applied as written.

B. Evolution of the Bankruptcy Rules

Having a grasp of the history of the Bankruptcy Rules is helpful in understanding the absence of a more complete discussion in the Committee Notes[69] and in understanding the Committee's failure to recognize that the rule is broad enough to prevent district court judges from exercising what has come to be considered by many as an inherent power.[70] The concept of having a formal, separately published set of rules to govern procedure in the bankruptcy courts is a relatively recent one.[71] Until 1976, when the final rules of the initial set of procedural rules were promulgated by the Supreme Court and became effective,[72] the Bankruptcy Act of 1898[73] contained all of the procedural, as well

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65. [A] COLLIER ON BANKRUPTCY app. pt. 2(b), at 2-122 (Lawrence P. King ed., 15th ed. rev. 2001).

66. One commentator has suggested that Rule 53 was made inapplicable to bankruptcy cases through Rule 9031 because of "the expense of special masters in bankruptcy, and . . . 'public perceptions of cronyism.'" Kauffman, *supra* note 35, at 171 n.82. Rule 53 has been construed as requiring the parties' consent. Where the creditors and the court agree that the special masters can preform certain tasks more efficiently, the creditors agree to bear that expense. The bankruptcy estate would not bear the cost. The expense of the special master should not be a concern because it would be incurred only if the parties consent.

67. *See supra* notes 56-58 and accompanying text.

68. *See infra* notes 85-89 and accompanying text.

69. *See supra* notes 58-59 and accompanying text.

70. *See infra* notes 131-43 and accompanying text.

71. *See generally* Lawrence P. King, *The History and Development of the Bankruptcy Rules*, 70 AM. BANKR. L.J. 217 (1996) (discussing in great detail the history and process of bankruptcy rulemaking).

72. *See* Bankruptcy Rules & Official Forms, 425 U.S. 1003 (1975); Bankruptcy Rules & Official Bankruptcy Forms, 411 U.S. 989, 991 (1972); King, *supra* note 71, at 220 (describing the decision to draft and promulgate the rules in parts, so that the

as the substantive provisions, of bankruptcy law.[74] Prior to that time, experience in drafting separate procedural rules for bankruptcy was extremely limited.[75]

In 1964, Congress granted bankruptcy rulemaking authority to the Supreme Court.[76] For the first time, it was possible to draft a complete set of rules to provide for all procedural matters that may arise in bankruptcy cases. The Advisory Committee charged with drafting the rules decided to approach this awesome task chapter by chapter.[77] As draft rules were completed by the Committee, they were disseminated to the bench and bar for comment. Finally, in April of 1976, after many years of tedious and faithful work by the Committee, the final set of rules were promulgated.[78]

The enactment of the Bankruptcy Code,[79] with its extensive changes to the bankruptcy laws, made revisions to the rules an absolute necessity. The Code was enacted in 1978 with an effective date of October 1, 1979, but it was not until January 1, 1979, that a new Advisory Committee began its work on the new set of rules. This gave the Advisory Committee a mere nine months to draft a new set of rules to complement extensively modified bankruptcy laws. Even with the existence of a model to follow, nine months was a very short time when

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effective dates of the first set of rules are different for different parts of the package of rules).

73. Bankruptcy Act of 1898, Pub. L. No. 55-171, 30 Stat. 544 (repealed 1978).

74. *See* King, *supra* note 71, at 217 ("At least seventy percent of the Bankruptcy Act, if not more, was procedural.").

75. *See* King, *supra* note 71, at 217-18. An Advisory Committee on Bankruptcy Rules was appointed in 1960 by the Chief Justice as Chair of the Judicial Conference of the United States to study the bankruptcy procedural rules contained in the General Orders in Bankruptcy and Official Forms and to recommend amendments. These committee members gained experience with drafting proposed rules, although the scope of their review was quite limited.

76. The statute read as follows:

> The Supreme Court shall have the power to prescribe by general rules, the forms of process, writs, pleadings, and motions, and the practice and procedure under the Bankruptcy Act. Such rules shall not abridge, enlarge, or modify any substantive right. Such rules shall not take effect until they have been reported to Congress by the Chief Justice at or after the beginning of a regular session thereof but not later than the first day of May and until the expiration of ninety days after they have been thus reported. All laws in conflict with such rules shall be of no further force or effect after such rules have taken effect.

Bankruptcy Act, Pub. L. No. 88-623, § 1, 78 Stat. 1001 (current version at 28 U.S.C. § 2075 (1994)).

77. King, *supra* note 71, at 224.

78. *See* Bankruptcy Rules and Official Bankruptcy Forms, 425 U.S. 1003 (1975).

79. 11 U.S.C. §§ 101-1330 (2000) (as enacted by the Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549 (1978)) [hereinafter Bankruptcy Code].

compared to the twelve years that the first Advisory Committee took to draft the initial set of rules.[80] In light of this short time period, the Advisory Committee decided that the best course of action was to draft a set of interim rules.[81] The sole goal of the Advisory Committee in drafting the interim rules was to fill the gaps between the new Code and the existing rules; this goal was completed in August of 1979.[82] These interim rules were adopted as local rules and were used between the effective date of the new Code and the promulgation of the replacement rules. No effort was made at that point to make a detailed study of the existing rules to determine which rules required modification or deletion in light of the broader range of cases that the bankruptcy court could hear under the Code.

The Advisory Committee then began its work on the permanent set of rules. During the time that the Committee was taking comments on the interim rules, the United States Supreme Court decided a landmark case, *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*[83] The far-reaching implications of this case caused concern among members of the bankruptcy bar and bench, who promptly turned their attention to it. No changes were made to the proposed permanent rules as a direct result of this case because the Committee did not think that the rules contained anything that pertained to jurisdiction and because it was hoped that proposed legislation would resolve the entire issue.[84] If the Committee had reviewed its work on the rules in light of the *Northern Pipeline* decision before sending them on to the Judicial Conference and the Supreme Court, it is possible that matters, like the appointment of special masters, might have been discussed more thoroughly and different decisions might have been made.

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80. King, *supra* note 71, at 220-33.

81. *See* King, *supra* note 71, at 237.

82. JUD. CONF. OF THE U.S., COMM. ON RULES OF PRAC. & PROC., PRELIMINARY DRAFT OF PROPOSED NEW BANKRUPTCY RULES AND OFFICIAL FORMS, xix (1982).

83. 458 U.S. 50 (1982). In this case, a Chapter 11 debtor filed suit in the bankruptcy court against Marathon for damages based on a breach of contract and warranty, as well as misrepresentation, coercion, and duress. *Id.* at 56. Under the Bankruptcy Act of 1898, this kind of action would have been outside of the jurisdiction of the bankruptcy court, and the proper place to bring the action would have been the state court. The Bankruptcy Code had broadened the jurisdiction of the bankruptcy court so that it had jurisdiction to hear this kind of claim—one that was not directly a part of the bankruptcy matter. *Id.* at 54-55. The Supreme Court held that this broadened jurisdiction unconstitutionally vested the bankruptcy judges with "judicial power" without granting them the protection of Article III status. *Id.* at 87.

84. H.R. 6978, 97th Cong. (2d Sess. 1982) (reintroduced in the 98th Congress as H.R. 3, 98th Cong. (1983)). Granting bankruptcy judges Article III status would have done much toward resolving the jurisdictional issue.

C. Evolution of the Bankruptcy Court

A discussion of the role and status of the bankruptcy judge under the Bankruptcy Act provides some background against which the prohibition against special masters in bankruptcy cases under the Code can be better understood. This is helpful in understanding why the Committee thought that there would be no need to make FRCP 53 applicable under the Code.

Until 1973 under the Bankruptcy Act, the person who presided over bankruptcy cases held the position of "referee in bankruptcy."[85] The "referee in bankruptcy" had limited jurisdiction over most bankruptcy cases. In Chapter X corporate reorganizations, the jurisdiction of the "referee in bankruptcy" was so limited that the "referee" served only as a special master to hear and report generally or upon specified matters to the district court judge.[86] When the "referee" acted in a Chapter X case, former Bankruptcy Rule 513 applied to make FRCP 53 applicable in those instances, rendering the "referee in bankruptcy" a special master appointed by the district court.[87] Under the Chandler Act of 1938,[88] the duties and workload of the "referee in bankruptcy" increased tremendously, but the jurisdiction of the court was still limited. In 1973, the title "referee in bankruptcy" was changed to "United States bankruptcy judge" due, in part, to recognition of the increased duties required of this

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85. *See* H.R. REP. NO. 95-595, at 8 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5963, 5969.

86. The Bankruptcy Act of 1898, ch. 541, § 117, 30 Stat. 544 (1898) (repealed 1978); *see, e.g.*, Faucher v. Lopez, 411 F.2d 992, 995 (9th Cir. 1969) (The district court appointed the bankruptcy referee as special master to decide issues of fraud in the bankruptcy case.).

87. FED. R. BANKR. P. 513 (repealed Aug. 1, 1983), *reprinted in* 12 COLLIER ON BANKRUPTCY, at 5-103 (James Wm. Moore & Lawrence P. King eds., 14th ed. 1978) ("If a reference is made in a bankruptcy case by a judge to a special master, the Federal Rules of Civil Procedure applicable to masters apply."); *see also* 12 COLLIER ON BANKRUPTCY ¶ 513.6, at 5-106 (James Wm. Moore & Lawrence P. King eds., 14th ed. 1978) (discussing the district court judge's retention of jurisdiction in Chapter X corporate reorganization proceedings and that judge's reference of a proceeding under Chapter X to a referee in bankruptcy acting as a special master). The court in *United States v. Manning*, 215 F. Supp. 272, 293 (W.D. La. 1963), described the role of the bankruptcy referee:

> Rule 53 of the Federal Rules of Civil Procedure allows a district court to appoint a 'standing' master for its district or a 'special master'. As used in [the] rules the word "master" includes a referee, an auditor, and an examiner. Rule 53.... A Referee in Bankruptcy has even more power than a master: he may render a binding judgment.

88. Chandler Act, ch. 575, § 60e, 52 Stat. 883 (1938) (repealed 1979).

position.[89] Nevertheless, the new bankruptcy judges still did not have any greater jurisdiction than before.

In 1978, Congress enacted dramatically new bankruptcy legislation, which created and conferred on the bankruptcy courts very broad jurisdiction.[90] One of Congress's goals in reforming the bankruptcy laws was to create more efficient procedures for administering bankruptcies. To achieve this goal, Congress chose to vest broad powers and jurisdiction directly in the bankruptcy courts.[91] Even before Congress had an opportunity to enact permanent Bankruptcy Rules to accompany its newly enacted Bankruptcy Code,[92] its efforts were very quickly and successfully challenged in the landmark *Northern Pipeline* case.[93] The Supreme Court in *Northern Pipeline* held that the jurisdictional provisions of the Bankruptcy Code of 1978 were unconstitutional primarily because the Code had vested Article III[94] judicial power in non-Article III judges—judges who lacked lifetime tenure and protection against salary diminution.[95] Under the Bankruptcy Code, Congress granted to the bankruptcy courts all of the usual powers of the district courts, including the power to hear jury trials and to issue final judgments that were binding and enforceable in the absence of an appeal.[96] The Supreme Court held that this grant of judicial power without a grant of Article III status was unconstitutional as a violation of the separation of powers.[97] After the *Northern Pipeline* decision, Congress enacted amendments to the Bankruptcy Code to address the jurisdictional issues raised by the case.[98] In the 1984 Amendments, Congress gave federal district courts

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89. FED. R. BANKR. P. 901(7) (repealed Aug. 1, 1983); *see* Joseph C. Zavatt, *The Use of Masters in Aid of the Court in Interlocutory Proceedings*, 22 F.R.D. 283, 285 (1958) ("Over the years since the Act of 1898, [the powers of referees in bankruptcy] (subject to review) have been extended . . . to the point where (since 1938) they have the power to grant or deny discharges—a power formerly reserved to the District Court Judge sitting as a bankruptcy court.").

90. *See supra* note 76.

91. *See generally* Charles J. Tabb, *The History of the Bankruptcy Laws in the United States*, 3 AM. BANKR. INST. REV. 5 (1995).

92. Bankruptcy Rules, 461 U.S. 973 (1982) (Permanent rules for the 1978 Bankruptcy Code were not promulgated until 1983.).

93. 458 U.S. 50 (1982).

94. *See supra* note 12.

95. *Northern Pipeline*, 458 U.S. at 63.

96. *See* 28 U.S.C. § 1471(b) (This Section was added by Act of Nov. 6, 1978, Pub. L. 95-598, 92 Stat. 2668 (1978), but did not become effective pursuant to § 402(b) of such Act.).

97. *Northern Pipeline*, 458 U.S. at 85.

98. Federal Judgeship Act of 1984, Pub. L. No. 98-353, 98 Stat. 378 (1984). The amendments to the Code to address the issues in *Northern Pipeline* took a considerable period of time, during which bankruptcy cases were in limbo. The obvious solution was

exclusive jurisdiction "over all cases under title 11" and nonexclusive jurisdiction "of all civil proceedings arising under title 11, or arising in or related to cases under title 11."[99] The district courts have exclusive jurisdiction, under

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to make the bankruptcy judges Article III judges, but this had been rejected during the enactment process of the Reform Act and continued to be opposed. In a later amendment to the Bankruptcy Code, however, Congress created a Bankruptcy Review Commission, which recommended Article III status for bankruptcy judges to increase the efficiency of the bankruptcy process. The Commission pointed to the costs caused by the Article I status of bankruptcy judges, including those primarily associated with the necessity of drawing jurisdictional lines between core and non-core proceedings, and those caused by the constitutional uncertainty over the definition of core proceedings. NAT'L BANKR. REV. COMM'N, BANKRUPTCY: THE NEXT TWENTY YEARS § 3.1, at 718, 722-24, 732-35, 737-39 (1997). Both before and after this recommendation, many commentators advocated Article III status for bankruptcy judges. *See, e.g.*, Susan Block-Lieb, *The Costs of a Non-Article III Bankruptcy Court System*, 72 AM. BANKR. L.J. 529, 544-46 (1998) (pointing to the costs caused by dividing bankruptcy jurisdiction between the district and bankruptcy courts, including the delays caused by the division, and the doctrinal and constitutional uncertainty caused, and advocating Article III status for bankruptcy judges); Christopher F. Carlton, *Greasing the Squeaky Wheels of Justice: Designing the Bankruptcy Courts of the Twenty-First Century*, 14 BYU J. PUB. L. 37, 45-46 (1999). In his article, Mr. Carlton examined several proposals to amend the Bankruptcy Code and recommended Article III status for bankruptcy judges. He quoted the legislative history of the Reform Act of 1978's discussion of granting Article III status to bankruptcy judges:

> [T]he Constitution suggests that an independent bankruptcy court must be created under Article III. Article III is the constitutional norm, and the limited circumstances in which the courts have permitted departure from the requirements of Article III are not present in the bankruptcy context. Even if they were present, the text of the Constitution and the case law indicate that a court created without regard to Article III most likely could not exercise the power needed by a bankruptcy court to carry out its proper functions . . . . Congress should establish the proposed bankruptcy court under Article III, with all of the protection that the Framers intended for an independent judiciary.

Carlton, *supra*, at 45 n.55 (quoting H.R. REP. NO. 95-598, at 390 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6000). *But see generally* Thomas E. Plank, *Why Bankruptcy Judges Need Not and Should Not Be Article III Judges*, 72 AM. BANKR. L.J. 567 (1998) (citing historical and constitutional policy reasons why Article I status is desirable for bankruptcy judges).

Granting Article III status to bankruptcy judges, however, would not resolve the problem of the appointment of special masters in bankruptcy. Rule 9031 prohibits the appointment of special masters in any bankruptcy case, whether before an Article III judge or not. *See supra* note 61-62 and accompanying text.

99. 28 U.S.C. § 1334(a)-(b) (1994) (granting district courts original and exclusive jurisdiction over "all cases under title 11," and original but not exclusive jurisdiction over "all civil proceedings arising under title 11, or arising in or related to cases under title

the 1984 Amendments, over all property of the bankruptcy estate wherever it is located.[100] Through these amendments, Congress chose to give broader jurisdiction over bankruptcy matters to the district courts. Congress dealt with the status of the bankruptcy judges by declaring that they constitute a "unit" of the district court called the bankruptcy court.[101] The district courts may refer all bankruptcy cases and proceedings within their jurisdiction to the bankruptcy courts,[102] but, under the 1984 Amendments, the proceedings are divided into "core" and "non-core" matters with bankruptcy judges being permitted to "hear and determine" the matter and enter final judgment only in the "core" proceedings.[103] During and after the time that *Northern Pipeline* was making its

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11"). "Case" refers to the procedure followed in the administration of the debtor's estate and "proceeding" refers to the disputes occurring during the bankruptcy case. *See* 1 COLLIER ON BANKRUPTCY ¶¶ 3.01[1][c][i]-[ii], at 3-20 to 3-27 (Lawrence P. King ed., 15th ed. rev. 2001).

100. 28 U.S.C. § 1334(e) (1994).

101. *See* 28 U.S.C. § 151 (1994). Section 151, "Designation of bankruptcy courts," states:

> In each judicial district, the bankruptcy judges in regular active service shall constitute a unit of the district court to be known as the bankruptcy court for that district. Each bankruptcy judge, as a judicial officer of the district court, may exercise the authority conferred under this chapter with respect to any action, suit, or proceeding and may preside alone and hold a regular or special session of the court, except as otherwise provided by law or by rule or order of the district court.

28 U.S.C. § 151 (1994).

102. 28 U.S.C. § 157(a) (1994). Section 157(a) states that: "Each district court may provide that any or all cases under title 11 and any or all proceedings arising under title 11 or arising in or related to a case under title 11 shall be referred to the bankruptcy judges for the district." 28 U.S.C. § 157(a) (1994).

103. 28 U.S.C. § 157(b)(1) (1994). Dividing the bankruptcy proceedings into "core" and "non-core" proceedings permitted Congress to allow bankruptcy judges to hear bankruptcy cases while maintaining Article I status without running afoul of *Marathon*. In its opinion in *Northern Pipeline*, the Court recognized an exception to the separation of powers that permitted Congress to set up legislative courts in specialized areas like bankruptcy where the adjudication of a "public right" is involved. The "core" matters involve issues directly related to the restructuring of the debtor-creditor relationship, the "public right;" these matters may be heard by the bankruptcy judge subject only to appeal. 28 U.S.C. § 158 (1994). Under 28 U.S.C. § 157(c)(1), there are circumstances under which bankruptcy judges may hear "non-core" proceedings:

> A bankruptcy judge may hear a proceeding that is not a core proceeding but that is otherwise related to a case under title 11. In such proceeding, the bankruptcy judge shall submit proposed findings of fact and conclusions of law to the district court, and any final order or judgment shall be entered by the district judge after considering the bankruptcy judge's proposed findings and conclusions and after reviewing *de novo* those matters to which any party

way to the Supreme Court, bankruptcy courts were operating under the rules adopted under the Bankruptcy Act and interim rules designed to fill the gaps between the Bankruptcy Code and the original rules under the Act.[104] The first permanent rules were being drafted for the new Bankruptcy Code at the same time as amendments were being made to the Code to address the *Northern Pipeline* jurisdictional issues.[105] These jurisdictional issues also needed to be addressed in the rules. It may have been the haste and confusion of the day that led to the unexplained conclusion that special masters could not be appointed in bankruptcy cases.[106] Whatever the reason, what resulted was Rule 9031 with its inadequately explained prohibition against the appointment of special masters in bankruptcy cases.[107] A court's inability to use as important a case management device as special masters hinges on Rule 9031, a rule with virtually no explanation or justification—and one that appears to have been drafted in haste, without significant consideration given to its significant impact.

V. NO COMPARABLE ROLE EXISTS

Special masters are appointed by the court to assist in cases where the issues are complicated and where exceptional conditions exist, or in matters of account and where there are difficult damages computations.[108] The special master is appointed to assist the court in cases in which the court deems help necessary to

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has timely and specifically objected.
28 U.S.C. § 157(c)(1) (1994).

104. *Committee on Rules of Practice and Procedure of the Judicial Conference of the United States*, *in* [A] COLLIER ON BANKRUPTCY app. pt. 2(b), at 2-116 to 2-119 (Lawrence P. King ed., 15th ed. rev. 2001).

105. *See supra* notes 83-84 and accompanying text.

106. *See generally* [A] COLLIER ON BANKRUPTCY app. pt. 2(b), at 2-122 (Lawrence P. King ed., 15th ed. rev. 2001).

107. The possibility exists that the Committee Notes were drafted with the former practice of having bankruptcy referees act as special masters in Chapter X cases under the former Bankruptcy Act in mind. At least one judge has suggested that Rule 9031 was drafted with this former practice in mind. *See In re* S. Portland Shipyard & Marine Rys. Corp., 32 B.R. 1012, 1020 n.9 (D. Me. 1983). The *In re S. Portland* court stated:

> Rule 9031 was enacted because the new Code, if left intact, would have made the reference of bankruptcy cases superfluous.... The new Code was not left intact, however; ... Rule 9031, which specifically addressed the situation in which all bankruptcy cases are to be heard by Bankruptcy Judges in the first instance, is incongruous in the situation created by *Northern Pipeline* whereby the District Court is to exercise bankruptcy jurisdiction.

Id. at 1021 n.10. The Committee never may have contemplated bankruptcy judges appointing special masters in bankruptcy cases.

108. FED. R. CIV. P. 53(a)-(b).

further the administration of justice.[109] The role of the special master is to represent the court in carrying out specified duties, as directed by the appointing court. The Bankruptcy Code does not provide for the appointment of a person in a comparable position. The Bankruptcy Code does provide for the appointment of trustees and examiners.[110] In fact, the Code mandates that, under certain circumstances, the court must appoint examiners and trustees after a request to do so[111] is made by a party in interest[112] or the United States Trustee.[113]

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109. *See Ex parte* Peterson, 253 U.S. 300, 312 (1920) (Justice Brandeis, referring to the role of the special master, stated that he or she is an "instrument for the administration of justice [to be employed by the court] when deemed by it essential."); United States v. Manning, 215 F. Supp. 272, 293 (W.D. La. 1963) (noting that the special master is charged with the same obligations of a judicial officer).

110. 11 U.S.C. §§ 704, 1104, 1106, 1202, 1302 (2000) (explaining the duties of a trustee in a Chapter 7 case, the appointment of a trustee or examiner in a Chapter 11 case, the duties of a trustee and examiner, and the duties of trustee in a Chapter 12 case, respectively). For an excellent discussion of the role of the examiner and a comparison of that role to that of the trustee, see Leonard L. Gumport, *The Bankruptcy Examiner*, 20 CAL. BANKR. J. 71 (1992).

111. 11 U.S.C. § 1104 (2000) provides in relevant part:

> (a) At any time after the commencement of the case but before confirmation of a plan, on request of a party in interest or the United States Trustee, and after notice and a hearing, the court shall order the appointment of a trustee—
>
> (1) for cause, including fraud, dishonesty, incompetence, or gross mismanagement of the affairs of the debtor by current management, either before or after the commencement of the case, or similar cause, but not including the number of holders of securities of the debtor or the amount of assets or liabilities of the debtor; or
>
> (2) if such appointment is in the interests of creditors, any equity security holders, and other interests of the estate, without regard to the number of holders of securities of the debtor or the amount of assets or liabilities of the debtor. . . .
>
> (c) If the court does not order the appointment of a trustee under this section, then at any time before the confirmation of a plan, on request of a party in interest or the United States trustee, and after notice and a hearing, the court shall order the appointment of an examiner to conduct such an investigation of the debtor as is appropriate, including an investigation of any allegations of fraud, dishonesty, incompetence, misconduct, mismanagement, or irregularity in the management of the affairs of the debtor of or by curent or former management of the debtor, if
>
> (1) such appointment is in the interests of creditors, any equity security holders, and other interests of the estate; or
>
> (2) the debtor's fixed, liquidated, unsecured debts, other than debts for goods, services, or taxes, or owing to an insider, exceed $5,000,000.

112. No definition for the term "party in interest" is provided in the Bankruptcy Code. Some guidance is provided in 11 U.S.C. § 102 (2000). The Legislative Statement

When they are appointed, trustees and examiners represent the bankruptcy estate, have very broad duties, and are required to perform comprehensive acts for the benefit of the entire estate,[114] such as accounting for property received,

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provides that: "[r]ules of bankruptcy procedure or court decisions will determine who is a party in interest for the particular purposes of the provision in question. . . ." 11 U.S.C. § 102 (2000).

113. 28 U.S.C. §§ 581-589 (1994) (These provisions describe the United States Trustee system, which was designed, in large part, to perform and oversee the administration of bankruptcy cases.).

114. 11 U.S.C. § 323(a) (2000) provides, in relevant part, that "[t]he trustee in a case under this title is the representative of the estate." 11 U.S.C. § 1106 (2000) provides, in relevant part:

> A trustee shall—
>
> (1) perform the duties of a trustee specified in sections 704(2), 704(5), 704(7), 704(8), and 704(9) of this title;
>
> (2) if the debtor has not done so, file the list, schedule, and statement required under section 521(1) of this title;
>
> (3) except to the extent that the court orders otherwise, 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;
>
> (4) as soon as practicable—
>
> (A) file a statement of any investigation conducted under paragraph (3) of this subsection, 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
>
> (B) transmit a copy or a summary of any such statement to any creditors' committee or equity security holders' committee, to any indenture trustee, and to such other entity as the court designates
>
> . . . .
>
> (b) An examiner appointed under section 1104(d) of this title shall perform the duties specified in paragraphs (3) and (4) of subsection (a) of this section, and, except to the extent that the court orders otherwise, any other duties of the trustee that the court orders the debtor in possession not to perform.

11 U.S.C. § 704 (2000) provides:

> The trustee shall—
>
> (1) collect and reduce to money the property of the estate for which such trustee serves, and close such estate as expeditiously as is compatible with the best interests of parties in interest;
>
> (2) be accountable for all property received;
>
> (3) ensure that the debtor shall perform his intention as specified in section 521(2)(B) of this title;
>
> (4) investigate the financial affairs of the debtor;
>
> (5) if a purpose would be served, examine proofs of claims and object

examining proofs of claims, furnishing information concerning the estate to parties in interest who have made requests, filing periodic reports of the operation of the business with taxing authorities, and making final reports to the court on the administration of the estate.[115]

In contrast, the special master is appointed by the court to represent the court by performing narrow, well-delineated tasks.[116] District courts order the special master to perform these well-delineated tasks in a very limited manner and for a specific proceeding within a case—not for the entire case.[117] Special masters have a different mission, different loyalties, and different supervisors than do trustees and examiners. Trustees and examiners are not authorized under the Code to perform the vast majority of tasks that a court would need and appoint a special master to perform.[118]

It is the general goal of all courts to conserve judicial resources and to enhance the efficiency of the court with regard to its case management.[119] Even as "units" of the district court,[120] bankruptcy courts share this same goal. Trustees and examiners, however, cannot help the bankruptcy courts in reaching this goal of conserving judicial resources and enhancing the efficiency of the courts with regard to case management. In Section 1104, where the Code provides for the appointment of trustees and examiners, there is nothing within

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to the allowance of any claim that is improper;
(6) if advisable, oppose the discharge of the debtor;
(7) unless the court orders otherwise, furnish such information concerning the estate and the estate's administration as is requested by a party in interest;
(8) 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; and
(9) make a final report and file a final account of the administration of the estate with the court and with the United States trustee.

115. 11 U.S.C. § 704 (2), (7), (8), (9) (2000).

116. *See supra* notes 14, 21-31, and accompanying text.

117. *See supra* note 14 and accompanying text. In fact, it is when courts have appointed a special master to perform tasks that amount to full and complete fact-finding in the case that courts find the appointment improper as a substitute for the judicial role.

118. Compare the duties of the trustee and examiner under 11 U.S.C. §§ 704, 1106, 1202, 1302 (2000), with the powers of the special master under FED. R. CIV. P. 53. *See also supra* notes 15-31 and accompanying text.

119. *See supra* notes 27-28 and accompanying text.

120. 28 U.S.C. § 151 (1994).

the outlined duties that would reflect the goal of providing assistance to the court.[121] There are alternate standards provided for the appointment of trustees and examiners,[122] and the trustee and the examiner have different duties; however, the appointment of these individuals is not designed to assist the courts in the management of the case.

The trustee's duties are to protect the debtor's assets for its creditors and equity security holders.[123] The trustee has broad powers to carry out this goal, including ousting the debtor's current management and operating the business directly. The examiner is appointed to conduct an investigation of the debtor.[124] The Code appears to contemplate that what the examiner will investigate is improper conduct by, toward, or involving the debtor.[125] The goal of the investigation by the examiner is directed at providing information about the feasibility and wisdom of the continued operation of the Chapter 11 debtor's business. The goal does not appear to be directed at the courts' management of the case as much as it is at the protection of the Chapter 11 debtor's creditors and equity security holders.[126] The examiner's investigation may provide information that ultimately effects the management of the cases; however, it is not the management of the case itself that the examiner's appointment is designed to effect.

Traditionally, special masters have been appointed in complicated two-party and class-action litigation.[127] In bankruptcy cases, particularly in proceedings brought to determine the dischargeability of debts[128] in complex commercial cases, problems related to the computation of damages may be quite complicated and may involve voluminous documents and repeated disputes among different claimants regarding quite similar matters, in much the same way as in two-party and class-action litigation. Although trustees and examiners may be appointed by the bankruptcy court,[129] the duties of the trustee and examiner as described in the Code[130] do not include providing case management assistance to the court in litigation matters like the discharge of debts, one of the very areas where complicated matters of account or computation are most likely to occur. In these

121. 11 U.S.C. § 1104(c) (2000).
122. 11 U.S.C. § 1104(a)(1), (c) (2000).
123. *See* 11 U.S.C. § 704 (2000).
124. 11 U.S.C. §§ 1104(c), 1106(a)(3)-(4), (b) (2000).
125. 11 U.S.C. § 1104(c) (2000).
126. 11 U.S.C. § 1104(c) (2000).
127. *See, e.g.*, Brazil, *Special Masters*, *supra* note 3.
128. 11 U.S.C. § 523(a)(1)-(16) (2000).
129. Examiners only may be appointed in Chapter 11 cases. *See* 11 U.S.C. §§ 103, 901 (2000).
130. *See supra* note 110 and accompanying text.

matters, the bankruptcy court is not authorized to appoint an individual with the expertise to assist the court in expediting these matters.

VI. INHERENT AUTHORITY OF COURTS OF EQUITY

The authority of courts to control and direct the business of the court in the interest of the sound and efficient administration of justice flows from the very nature of a judicial body and requires no grant of power other than that which creates the court and gives it jurisdiction. In fact, much of what courts must do in the conduct of their business is not provided for in any rule or statute and necessarily relies on inherent authority. The court's inherent authority to direct its business in the interest of the efficient administration of justice provides courts with significant leeway in conducting the business of the court. This inherent authority is well established and widely accepted in the federal judiciary.[131]

The historical development of the courts' authority to appoint special masters began in English courts of equity.[132] In this country, former Equity Rule 68, "Appointment and Compensation of Master," and former Equity Rule 59, "Reference to Master—Exception, Not Usual," provided the first statutory basis for the appointment of special masters; FRCP 53 developed as a modification of those rules.[133] Courts and commentators have emphasized that beyond FRCP 53, courts of equity have the inherent power to appoint special masters.[134] While

131. *See, e.g.*, Veneri v. Draper, 22 F.2d 33, 35 (4th Cir. 1927) ("There can be no question, we think, that under the federal practice the judge has the power in a proper case to refer a cause to an auditor for the purpose of simplifying the issues and thereby enabling the court and the jury to more readily determine the matters in dispute."); United States v. Conservation Chem. Co., 106 F.R.D. 210, 217-21 (W.D. Mo. 1985) (citing and reviewing numerous cases in which special masters were appointed to assist the court in various ways); Jordan v. Wolke, 75 F.R.D. 696, 701 (E.D. Wis. 1977) (appointing a special master pursuant to its inherent authority); Farrell, *Coping with Scientific Evidence*, *supra* note 3, at 943-44; Jacob, *supra* note 3, at 34.

132. *See supra* text accompanying notes 4-5.

133. Rules of Practice for the Courts of Equity of the United States, 42 U.S. (1 How.) xli-lxx (1842).

134. *See, e.g.*, *Ex parte* Peterson, 253 U.S. 300, 312 (1920) ("Courts have . . . inherent power to provide themselves with appropriate instruments required for the performance of their duties. This power includes authority to appoint persons unconnected with the court to aid judges in the performance of specific judicial duties, as they may arise in the progress of a cause."); Ruiz v. Estelle, 679 F.2d 1115, 1161 (5th Cir. 1982) (The federal courts' equitable power to appoint special masters to supervise implementation of decrees long has been established.), *cert. denied*, 460 U.S. 1042 (1983); Schwimmer v. United States, 232 F.2d 855, 865 (8th Cir. 1956) ("Beyond the provisions of Rule 53, Federal Rules of Civil Procedure, 28 U.S.C.A., for appointing and

some commentators have suggested that FRCP 53 is not applicable to pretrial phases of a civil lawsuit, they have observed that federal courts may have the power to appoint a special master in pretrial matters under their inherent authority.[135]

The fact that the federal courts' inherent authority to appoint special masters existed prior to FRCP 53 has been throughly researched and discussed by Wayne D. Brazil.[136] He noted that "the Advisory Committee's intent in drafting Rule 53 was to preserve the essentials of the system of referencing as it existed under the Federal Equity Rules between 1912 and 1938."[137] The "essentials of the system," as they relate to the duties of the special master, included appointing special masters to assist the courts by gathering and analyzing relevant data from complex financial records and making recommendations to the court, to aid in computing damages and in providing other well-defined assistance on specific, narrow issues.[138]

This is exactly the kind of assistance that bankruptcy courts need—assistance in performing very specific and well-focused tasks.[139] Bankruptcy courts are recognized as courts of equity,[140] and, as such, they have the inherent authority to appoint special masters to perform these same specific, narrow, well-defined tasks that special masters were appointed to perform by

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making references to Masters, a Federal District Court has 'the inherent power to supply itself with this instrument for the administration of justice when deemed by it essential.'" (quoting *Peterson*, 253 U.S. at 312)); Westchester Fire Ins. Co. v. Bringle, 86 F.2d 262, 263 (6th Cir. 1936); Jordan v. Wolke, 75 F.R.D. 696, 701 (E.D. Wis. 1977) ("This appointment [of a special master] is made pursuant to the court's general equity powers and not under Rule 53, Federal Rules of Civil Procedure."); Conn. Importing Co. v. Frankfort Distilleries, Inc., 42 F. Supp. 225, 226 (D. Conn. 1940) ("The power of the court so to proceed [to appoint a special master] is beyond question. It exists independent of the rule. Rule 53 serves but to outline the procedure to be followed when the power is exercised."); Thompson v. Smith, 23 F. Cas. 1092, 1093 (C.C. Ohio 1869) ("[A]cted under the authority of a well-established principle, that the courts of the United States, in the exercise of their chancery powers, possess an inherent authority, in proper cases, to order a reference to a master."); Kaufman, *supra* note 5, at 462 ("There has always existed in the federal courts an inherent authority to appoint masters. . . .").

135. *See generally* MANUAL FOR COMPLEX LITIGATION § 20.14, at 16 (3d ed. 1982); Brazil, *Referring Discovery Tasks*, *supra* note 17, at 143.

136. Brazil, *Referring Discovery Tasks*, *supra* note 17, at 149-60.

137. Brazil, *Referring Discovery Tasks*, *supra* note 17, at 149 (citing statements of Robert G. Dodge, a member of the original Advisory Committee, and Edgar B. Tolman, the secretary of the Advisory Committee on the rules for civil procedure).

138. Brazil, *Referring Discovery Tasks*, *supra* note 17, at 155.

139. *See supra* notes 33-41 and accompanying text.

140. *See* Curtis v. Loether, 415 U.S. 189, 195 (1974); Bank of Marin v. England, 385 U.S. 99, 103 (1966).

courts of equity prior to the enactment of FRCP 53. Bankruptcy courts have not relied upon this inherent authority to appoint special masters presumably because of the existence of Rule 9031.[141]

The only current prohibition against the appointment of a special master in bankruptcy is this procedural rule. There is no statutory provision within the Bankruptcy Code that prohibits the appointment of special masters. The Code expressly prohibits the appointment of receivers[142] through a specific statutory

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141. Significant controversy exists regarding the relationship between written procedural rules and inherent judicial authority, and the extent to which procedural rules can and should limit courts' inherent authority over their process and procedure. The fact that a procedural rule addresses specific issues does not necessarily mean that a court successfully cannot assert its inherent authority to allow it to deal with those same issues. Courts sometimes find that the rules can be interpreted so that pre-existing inherent authority simply supplements the rules. *See, e.g.*, Chambers v. NASCO, Inc., 501 U.S. 32, 46 (1991); Link v. Wabash R.R., 370 U.S. 626, 629-33 (1962) (holding that FED. R. CIV. P. 41(b) authorizing dismissals on the motion of the defendant did not deprive courts of their inherent authority to dismiss without such a motion). The Court in *Chambers* rejected the argument that the sanction provisions of FED. R. CIV. P. 11 and 28 U.S.C. § 1927 restrict the court's inherent authority, and stated:

> We discern no basis for holding that the sanctioning scheme of the statute and the rules displaces the inherent power to impose sanctions for the bad-faith conduct [in this case]. These other mechanisms, taken alone or together, are not substitutes for the inherent power, for that power is both broader and narrower than other means of imposing sanctions.

Chambers, 501 U.S. at 46. *But see* Brooks Fashion Stores v. Mich. Employment Sec. Comm'n, 124 B.R. 436, 440 (Bankr. S.D.N.Y. 1991) ("The Bankruptcy Rules were promulgated by the Supreme Court pursuant to authority granted by Congress in 28 U.S.C. § 2075. As such, the Rules have the force of law."); John Papachristo, Comment, *Inherent Power Found, Rule 11 Lost: Taking a Short Cut to Impose Sanctions in* Chambers v. NASCO, 59 BROOK. L. REV. 1225, 1250-65 (1993) (arguing that the rules should be construed generally to pre-empt inherent authority).

Bankruptcy judges have not appointed special masters routinely pursuant to the inherent equitable powers granted the bankruptcy court under Bankruptcy Code § 105(a): "[t]he court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title." 11 U.S.C. § 105(a) (2000). Although § 105 serves as the depository of the bankruptcy court's inherent equitable powers, vesting the court with the power to issue orders necessary to carry out the provisions of the Bankruptcy Code, bankruptcy judges apparently have felt constrained by Rule 9031.

142. 11 U.S.C. § 105(b) (2000) ("Notwithstanding subsection (a) of this section, a court may not appoint a receiver in a case under this title."). Under the former Act, the bankruptcy judge had the power to appoint receivers in bankruptcy cases, but the Bankruptcy Code replaced the role of the receiver in bankruptcy with the interim trustee. Under the Bankruptcy Code, there no longer was a need to appoint the receiver as under the former law. *See generally* BENJAMIN WEINTRAUB & ALAN N. RESNICK, BANKRUPTCY LAW MANUAL ¶ 6.02, at 6-4 to 6-7 (3d ed. 1992).

provision. If the drafters had specific and strong reasons why special masters should not be appointed in bankruptcy cases, it is likely that they would have drafted an express statutory provision, as opposed to a procedural rule, as they did regarding receivers.[143] However, the drafters failed to do so.

VII. CONCLUSION

There are many reasons to permit bankruptcy courts to benefit from the unique services of special masters in the unusually complex bankruptcy case or proceeding—chief among them is an interest in the sound and efficient administration of justice. There are very few sound reasons to deny bankruptcy courts the benefit of special masters. In fact, Rule 9031, which is the sole prohibition against the appointment of special masters in bankruptcy cases, cites no reason at all for denying courts the benefit of this well-accepted case management device.

Many authorities have concluded that no express statutory basis is required for courts of equity to appoint a special master.[144] These authorities hold that courts of equity have inherent power and authority to do that which is necessary to carry out their duties, including appointing persons unconnected with the case to assist the courts in performing their duties.[145]

The effect of Federal Rule of Bankruptcy Procedure 9031 is to deny both the district court and the bankruptcy court the right to appoint a special master in appropriate cases. In denying these courts the power to appoint special masters in bankruptcy cases, Rule 9031 abridges the inherent power of both the district court and the bankruptcy court to act as courts of equity by employing a traditional tool available to a court of equity.[146] But, more significantly, it deprives debtors and creditors of the opportunity to benefit from this traditional judicial resource.

Congress expressly has authorized the Supreme Court to prescribe rules for the Bankruptcy Court.[147] However, in authorizing the Court to prescribe these rules, Congress provided that: "[s]uch rules shall not abridge, enlarge, or modify any substantive right."[148] The inherent power of courts to appoint special masters is a long-standing and well-accepted substantive right that, arguably, has been impermissibly abridged by this procedural rule. A procedural rule should

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143. 11 U.S.C. § 105(b) (2000).

144. *See supra* notes 131-38 and accompanying text.

145. *See supra* notes 131-38 and accompanying text.

146. *See supra* notes 131-38 and accompanying text.

147. 28 U.S.C. § 2075 (1994) ("The Supreme Court shall have the power to prescribe by general rules, the forms of process, writs, pleadings, and motions, and the practice and procedure in cases under Title 11.").

148. 28 U.S.C. § 2075 (1994).

not function in a way that, even arguably, modifies an inherent right of the court.[149] Rule 9031 should be abrogated, and a new rule that would permit the appointment of special masters in bankruptcy cases consistent with the substantive rights of a court of equity should be promulgated.

149. *See In re* Oliver, 452 F.2d 111, 114 (7th Cir. 1971) ("[N]o rule of court can enlarge or restrict jurisdiction. Nor can a rule abrogate or modify the substantive law.").

some sitting Bankruptcy Judges who act as “settlement judges” (a fancy name for mediator) who serve at no cost to the parties. The parties need merely to ask for the appointment of a settlement judge and the Court’s virtually always accommodate. In the alternative if the parties identify a particular member of the panel, then the Court will usually appoint the choice of the parties.

4. Mediation is not the same as judicial settlement conference as discussed by in Factors Influencing A Successful Mediation, Constr. Law., SUMMER 2002, at 18

a) Mediation is a much more sophisticated process than it may appear on the surface. It should not be confused with the judicial pretrial settlement conference, the most common experience most lawyers have with the use of neutrals. Mediation puts a primary emphasis on the client as decision maker and should be designed to address the expectations, fears, and emotional needs of the client. Judicial settlement conferences place primacy on the lawyer-advocate and the judge.

b) In mediation, the client is exposed to the important facts of the case and makes an assessment of risks and rewards without those facts being filtered through the bias of an advocate lawyer. Competent lawyers may have an emotional attachment to their client's cause, which can interfere with their ability to objectively assess the probabilities of success. In judicial settlement conferences, the stakeholders may not even be present.

c) In mediation, lawyers and their clients are able to engage in a confidential dialogue with the mediator about their economic needs without the fear of disclosure of information or a fear that the disclosed information will adversely affect the outcome if the case is not settled. Neither party subsequently can call the mediator to testify in court or at arbitration. Parties are often unwilling to be frank to a judge who may try their case. If the settlement judge is not the trial judge, he or she often lacks persuasive powers.

d) Judicial settlement conferences usually occur after costly discovery has occurred. In a mediation, the outcome-determinative facts are cooperatively shared between the parties without the need for costly formal discovery. This is often a side benefit of mediation that would not come out of a meeting with a settlement judge. Many lawyers believe that they can learn enough from a failed mediation to try a case with a minimal amount of additional discovery.[footnotes omitted]

5. It is important the parties have confidence in the person appointed to act as mediator, so that knowledge of commercial finance, bankruptcy, secured transactions, financing and ancillary agreements and as well as the substantive legal areas. Not all of the panelists have broadly based business finance experience; however, there seems to be a lack of uniformity as to ADR programs.

6. Outside of Bankruptcy, the use of ADR programs varies widely from state to state, particularly in foreclosures and commercial lending disputes as well as

consumer credit cases. Many states have enacted consumer foreclosure mediation statutes, as summarized in Appendix 1[2]. There are any other state laws requiring mediation, particularly in consumer matter. One must research the particular matter in the relevant state to determine if there is a mandatory mediation requirement in your particular case.

7. Clearly, the use of mediators is very common in many types of debtor-creditor cases that often lead to bankruptcy filings.

VII. Mediation vs Arbitration

A. This paper does not attempt to cover mandatory arbitration which is often contractually mandated in many types of debtor-creditor matters. Indeed, the enforceability of mandatory arbitration proceedings are the subject of the Federal Arbitration Act and a number of reported Circuit and Supreme Court cases. The topic of arbitration is far beyond the scope of this seminar section, therefore this section will focus solely upon the use of neutrals in the role of mediator. To focus or discussion, it is important to understand the difference between mediation and arbitration. Briefly, the difference between mediation and arbitration was well summarized Reaching the Settlement[3] § 2:7

B. There is a big difference between *mediation* and *arbitration*. Mediation is the process by which an independent and neutral professional oversees the negotiation process and tries to bring the parties to a voluntary resolution. That is, the mediator is an

[2] Courtesy of the Nation Consumer Law Center.
[3] Negotiating and Settling Tort Cases: Reaching the Settlement, March 2018 Update, Guy O. Kornblum, Esq. West Publishing.

intermediary between the parties who tries to obtain an agreed upon resolution of a dispute to avoid the matter being decided by a court, jury or arbitrator. That resolution does not occur unless the parties agree. The mediator has experience and training in the negotiation process and facilitates a dialogue between the disputants in an effort to find an acceptable compromise. It is important to understand that mediation is a process of *compromise*. In order to have a hope of a resolution, the parties must be willing to negotiate through the mediator and participate in the give and take of negotiation. But again, nothing happens unless the parties agree to a resolution. If they do not, the matter continues through the dispute resolution process, either in court or through an alternative manner, such as arbitration.

C. *Arbitration* is <u>not</u> a process of negotiation. It involves a neutral who decides the case, much like a judge would do. This neutral is either agreed upon by the parties, or is chosen by a local judge. Sometimes a contract will provide for three arbitrators with each side to choose one, and the two party arbitrators select a neutral who serves as the presiding officer for the arbitration hearing.

D. Participants in mediation typically include a neutral, the parties themselves, and the respective parties attorneys. Through a series of meetings with the parties, some of which are joint and some of which are caucuses with the individual parties, a mediator is often able to facilitate resolution of a dispute that is acceptable to all parties where the parties have been unable to reach a resolution on their own. The mediator assists the parties facilitating communications, guiding the parties to focus on their real underlying interests, and attempting to find a mutually acceptable solution for all.

E. Compared to traditional court litigation, it is usually much faster and far less expensive. Court litigation in commercial matter is generally open to the world, while mediation private and confidential. Court litigation tends to increase the level of animosity while galvanizing the parties opposing views and position, none of which helps when the parties attempt to negotiation an agreement on their own.

F. On the other hand, the parties to a mediation rather than a court retain control over the process. Mediation offer an environment which foster a creative resolution that is more creative than the winner take all outcome common in litigated decision. The mediation process allows the parties to vent their emotions before a third party, and sometimes each other, in effect have a "day in court"; yet, because mediation is confidential, consensual, and takes place in a less formal environment than a courtroom but with a neutral third party present, animosity usually subsides and many times the parties relationships can be preserved. Because clients are more directly involved in the mediation process as compared to court litigation, the business interests are more readily identified and tend to focus the process of reaching of business-oriented solutions.

VIII. Starting the process.

A. Mediation usually begins in one of two ways. Either the parties agree to participate in mediation or the court mandates participation. Agreements to participate in mediation may arise at the inception of the parties relationship by the inclusion of contractual provisions requiring the parties to mediate disputes between them prior to commencing litigation. In the alternative where there is not such contractual mediation process, then when a dispute arises, the parties may agree at any time, either before or after litigation commences, to mediate the dispute.

B. Additionally, the courts sponsor mediation programs. Although these programs often lack the flexibility of voluntary mediation, and in particular, may inhibit the parties' abilities to retain a mediator with the skills and qualifications necessary to resolve the disputed issues, many courts now as part of the pretrial process order mediation.

C. The ground rules for mediation by agreement are set forth completely in the mediation agreement entered into by the parties. These agreements ordinarily include the following terms[4]:

- The mediation process is voluntary.
- The mediation process is nonbinding.
- Either party may withdraw from the mediation at any time.
- The mediator shall be neutral and impartial.
- The mediator shall be agreed on by the parties.
- The mediator has complete discretion to control the mediation process.
- The mediator is free to meet and communicate separately with each party.
- The parties may not communicate with each other regarding the dispute without the consent of the mediator.
- The parties may but need not be represented by an attorney.
- The mediation process will be conducted expeditiously.
- At least one person with authority to resolve the dispute will be present on behalf of each party during the mediation.
- The mediator will not provide any information from a party to any other party unless expressly authorized to do so.
- The parties will not litigate during the mediation process.

[4] Business Workouts Manual § 23:18

- The mediator may not be called as a witness or consultant in any pending or future investigation or litigation.
- All information provided in the mediation is strictly confidential.
- The parties and the mediator agree not to disclose to any person information obtained in the mediation process.
- The parties jointly agree to pay the costs of the mediation.

D. Federal court mediation programs are authorized under Rule 16 of the Federal Rules of Civil Procedure. Rule 16(a)(5) states that facilitating settlement is one of five objectives of a pretrial conference. Under Rule 16, many federal courts have developed ADR processes including mediation orders or local rules that facilitate voluntary mediation. For bankruptcy cases, Bankruptcy Rule 7016 incorporates Federal Rule of Civil Procedure 16 for all adversary proceedings. For contested matters under Rule 9014 that are not adversary proceedings under Rule 7001, mediation is authorized through district court rules promulgated under Bankruptcy Rule 9029. Pursuant to these provisions, numerous district courts have adopted mediation procedures for bankruptcy proceedings.

IX. Why use a neutral/mediator?

A. The primary reason to use mediation is that it frequently is an efficient means to resolve a dispute. Why is this true? Unlike court litigation, mediation does not mandate a "win-lose" outcome common with court disposition where the result is typically money judgment based on notions of right and wrong. Mediation affords an opportunity for a business-oriented resolution with highly flexible terms based on the business needs of the parties. In mediation, the parties have far greater flexibility to fashion a solution that works for all.

B. An additional significant factor is that the clients are far more involved in mediation than in court litigation. Court litigation is regulated by a complex set of rules usually understood only by the lawyers who must resolve the case through the discovery process and a court decision after summary judgment or trial. It seems pretty common that a money judgment for one side does not really solve the problem at hand. On the other hand, in mediation, the clients and their counsel with the aid of a mediator often sit face to face across a conference table which frequently facilitates a business solution which actually solves a business problem.

C. Lastly, the mediation process is in and of itself focused on reaching an agreed resolution of a dispute whereas court ligation is focused on presenting facts to achieve prima facie case under a particular statute or common law claim for relief. The goal of mediation is for the parties to negotiate an agreed resolution. “The process is designed to allow them to vent their emotions, face the realities of their positions, focus on their true underlying business interests as opposed to merely "winning," and arrive at a solution that satisfies business as opposed to legal or emotional goals. This process is far less hostile and adversarial than litigation. Witness examinations in depositions and in court and other, often burdensome discovery that create hostility and harden the parties' positions do not occur in mediation. Because mediation is more low key, and much more focused on resolving a dispute rather than winning the case, anger and tension are minimized and the parties are more able to arrive at a creative business-oriented solution.

Thus, mediation allows parties to satisfy their business interests in a direct, efficient way."[5]

X. What is the role of a mediator?

A. The role of a mediator is quite different when compared to a judge in court litigation. Judges focus on the procedural rules of pleadings and discovery to move the case to a posture when it can be disposed of based on the relevant law applied to the facts, either by a trial or summary judgment. The mediator has a different set of tasks to accomplish.

B. The process of mediation, when conducted by an experienced mediator offers a much broader range of options to the table. On the other hand, a judge typically has a much more limited range of options and is often time left with merely declaring a winner and loser. The skilled mediator frequently will ascertain options the parties would have never considered thereby promoting a wider range of optional solutions for the parties which often results in a better solution.

C. Initially, the mediator will inquire into both sides' positions to bring to light the underlying business interests of each side. This process will assist each party to highlight their primary interests rather than just trying to win in court and thereby assist the parties in attaining a acceptable business solution.

D. Once the mediator understands the position of the parties, then they can facilitate the parties understanding or the opposition's business interests viewed through the objective lens of the mediator. By so doing, the mediator facilitates a mutual

[5] Business Workouts Manual § 23:20

understanding of the competing interests of the opposing parties and thereby facilitate more reasoned negotiation of the respective parties actual interests, rather that the posturing and saber rattling that goes on in a typical court proceeding. Along these same lines, the mediator seeks to diffuse and deescalate the animosity and conflict that attends most lawsuits to create an environment of reasonable negotiation rather than the chess moves attendant to litigation.

E. An experienced mediator often is able to temper the expectations of the parties. Many times, the client has only heard their attorney's predictions as to the outcome of a trial. The mediator is able to offer a honest and confidential evaluation of the parties case necessary to bring an unreasonable parties or one with an unrealistic opinion of their case back to reality to facilitate a to a reasonable resolution of a dispute.

XI. Use of mediation in Bankruptcy Cases.

A. The use of mediation in bankruptcy cases appears to be both increasing and evolving. Mediation is often used in virtually any type of adversary proceeding or contested matter in the bankruptcy courts. Adversary proceedings are for the most part a civil suit conducted by the Bankruptcy Court and involve the many varied legal issues often touching on both bankruptcy and non-bankruptcy law issues. Adversary proceedings are appropriate for mediation just like any other sort of civil litigation.

B. Although contested matters are by their nature more narrow in scope and proceed on a more abbreviated time line that adversary proceedings, but often times still merit consideration for mediation in the certain cases.

C. For example, motions for relief from stay are often brought early in Chapter 11 cases. In larger or more complex cases star relief motion can be outcome determinative for the entire case and are usually the subject of substantial dispute. Such motions, either directly or tangentially, usually involve issues relating to the value of a creditor's collateral, the value of the debtor's other assets, and the rights of other creditors and third parties in that collateral and assets. Moreover, behind most relief-from-stay proceedings lies the issue of whether the debtor has a reasonable possibility of proposing a confirmable plan of reorganization. Such a motion typically involves discovery, expert witnesses and multi-day hearings which can result in substantial fees and expenses for all parties to the dispute. A negotiated resolution of such a motion is often times considerably better for everyone that a court decision to terminate the stay or deny such relief. Consequently, a hotly contested motion for relief from stay in a complex case is well suited for mediation and frequently results in a solution that grants the Debtor a chance to get a plan confirmed, but on terms and conditions not found in the Bankruptcy Code.

D. Mediation-appropriate issues are not limited solely to relief-from-stay proceedings but can also be very helpful in the plan confirmation process. The process of obtain plan confirmation is . Similar issues arise in various proceedings in Chapter 11 cases, ranging from the initial cash collateral battles to the confirmation hearing itself. Indeed, throughout a Chapter 11 case, disputes arise that may determine, directly or indirectly, whether the debtor can continue in business and whether the debtor can reorganize. Therefore, each of these disputes, from the initial cash collateral proceeding through the confirmation hearing, may affect many or all of the parties that have interests

in the Chapter 11. Because these many interests may be affected, mediation is an appropriate way to deal with the disputes among them and has been described as a process whereby each constituent group is given a stick, then locked in a room to beat each other until they come to an agreement[6]. The legal and factual basis for Chapter 11 Plan, plus the substantial creativity of good debtor's counsel when opposed by equally creative creditors' counsel generate very complex disputes which beg for a solution based on economics and business considerations. As such, disputed plan confirmations are well suited to mediation.

XII. When to mediate?

A. Mediation is appropriate at the earliest stage in a bankruptcy case, or any other case for that matter, when it becomes apparent the parties are going to have an active dispute. Early mediation can help avoid the expense of litigating disputes and help introduce an atmosphere of cooperation into as otherwise disputed bankruptcy case.

B. As the case progresses, mediation may also become very useful when "holdout" parties surface. The confidential and non-adversarial mediation environment when coupled with an experienced mediation can be particularly effective in reaching an agreement with parties who have unrealistic expectations or who perceive themselves to be in a blocking position for the case to proceed. Mediation may also be needed in presenting a workout plan in difficult and complicated cases where a plan suggested by a neutral third party is the only plan not perceived of as favoring particular interests.

[6] This statement has been attributed to Ken Klee, although verification was not successful.

XIII. Selection of mediator.

A. To have any chance of success, the person chosen to act as mediator must be completely neutral as a matter of fact and perception. In this context, the best test is that they must be a "disinterested person" as that term is defined in 11 U.S.C. §101(14). The best practice is to select a person who is also experienced in mediation generally and with particular experience and training in bankruptcy matters. A mediator who meets these standards will be in the best position for reality checking, credible position analysis, and creative exploration of options available to the parties individually and as a group.

B. A thoughtful and detailed discussion of the selection of a mediator is found in Factors Influencing A Successful Mediation, Constr. Law., SUMMER 2002, at 18, 18–19

1. The choice of the appropriate mediator can be a very important factor affecting the outcome of the mediation. The parties' lawyers usually make the selection. Unfortunately, that selection is often based only on superficial information gathered through inquiries to colleagues and acquaintances. Typically the inquiry is simply: "Is anyone familiar with Mediator X?" The answer is often the equally general, "Yes, Mediator X is good." Often mediators are selected because they have been a judge or arbitrator.

2. The parties, however, should engage in a more exhaustive and sophisticated investigation. A more proper inquiry would probe the following factors:

a) Is the mediator a respected authority for the business and technical situation in dispute? Are accounting, scheduling, or insurance issues important to

the outcome, and if so, how capable is this mediator of handling those issues? It is a common view that subject matter expertise is not an important mediator characteristic. However, expertise in the subject matter of the dispute can be important to give credibility to the mediator when assisting the parties in evaluating the strengths and weaknesses of their positions.

b) What kind of training in mediation technique has the mediator received? This is a particularly important criterion for former judges who often are overly evaluative in style. Effective training puts the mediator in touch with his or her natural biases and old habits.

c) Does the mediator understand why process design is the first and most important step? What kinds of procedures does the mediator utilize to encourage the exchange of information prior to a formal mediation session? Good mediators ask the parties for confidential memos that probe the unique factors of the dispute. These are followed up by telephone conversations with the lawyers to ensure that the necessary parties attend the mediation and that all the decision makers understand the important facts in dispute.

d) What are the interpersonal skills of the mediator? Is he or she good at "reading" people? Can the mediator understand any cultural differences at play? Good mediators can glean what people really mean and not merely rely on what they say. For example, where there are major personality clashes, an experienced mediator may determine that traditional public sessions may be unwise and offer an alternative method.

e) What is the mediator's track record? Most mediators will supply references. Arbitrators can do a good job of describing their qualifications on paper, but paper credentials are not fully revealing of the skills and styles of a mediator.

f) Is the mediator optimistic by nature? Optimistic mediators set the tone of mediation toward a successful resolution. Does the mediator work hard and is he or she willing to put in long hours if necessary? It is not unusual for settlement breakthroughs to occur late in the day of the mediation. If so, it is often better to continue the mediation into the evening, rather than send the parties home to return another day. The mediator must commit to the process and convince the lawyers and parties to do likewise.

g) Is the mediator creative? Often cases settle because the facts are put in a new light by the mediator. The mediator may help the parties explore noncash considerations as a medium of exchange, such as future work, discounts, or referrals. Innovative mediators are constantly on the lookout for ideas to break impasses.

h) What is the mediator's style? A common misconception is that a mediator should have either a “facilitative” or “evaluative” style. Facilitative mediators do not express an opinion on the merits of the disputes. Evaluative mediators view their role much like that of a judge— they hear a summary of the arguments and then express an opinion as to who wins and who loses. Mediators who are overly evaluative should be avoided in construction mediation. Good mediators do form

opinions. However, they view their role as one of educating and guiding the parties to an understanding of how a judge, jury, or arbitrator may view the facts and the law of their case. These mediators offer evaluations only with the consent of the parties and after other tactics have failed.

i) It is not unusual that lawyers making the selection of the mediator do not understand the best style of mediator for their clients. The parties choose mediation because they think that they can convince an evaluative style mediator, such as a former judge, of the correctness of their position. They believe that such an opinion will cause the case to settle. The reality is if that opinion is obtained, and it is adverse to the client, the client finds ways to rationalize not accepting the opinion. The party adversely affected by such a public evaluation often loses trust in the mediator and faith in the mediation process.[footnotes omitted].

C. Thoughtful consideration of the person to serve as mediator is well worth the time and effort as well as greatly increasing the odds of a successful resolution.

XIV. Conclusion.

When used with a carefully selected person to serve as mediator, the process of mediation can often result in a cost effective means to reach a more practical and ultimately satisfactory solution to many bankruptcy issues.