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One Size Fits None: An Overdue Reform for Chapter 7 Trustees

ABSTRACT. Despite their differences, consumer and business Chapter 7 cases are administered by the same trustees under the same rules. This Note advances four normative arguments against this one-size-fits-all approach, using novel empirical research to emphasize its shortcomings. First, human debtors have rights that artificial entities do not. Second, trustees create different socioeconomic value for consumers and businesses. Third, trustees' day-to-day work differs significantly across case types. Finally, trustees receive far less judicial oversight in consumer cases. Accordingly, this Note proposes two policy changes: (1) trustee compensation should differ for consumer and business cases, and (2) trustees should be allowed to specialize accordingly.

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INTRODUCTION

Bankruptcy law frequently treats businesses and consumers differently. For example, when using bankruptcy for the purposes of restructuring, corporations avail themselves of Chapter 11, while consumers avail themselves of Chapter 13. Under Chapter 11, corporations usually act as their own trustees (as debtors-in-possession), with Chapter 11 trustees available should the need arise.¹ Consumer bankruptcies are always overseen by Chapter 13 trustees who are wholly separate from the consumer undergoing bankruptcy. These sets of trustees are *different*. The rules and standards that govern them are *different*. This follows from the fact that corporations and consumers require *different* treatment.

Chapter 7 defies this conventional wisdom. In stark contrast to the rest of bankruptcy law, Chapter 7 administers business and consumer bankruptcies using the *same* set of trustees. It commands these trustees to apply roughly the *same* set of rules to business and consumer debtors. This entangling of business and consumer bankruptcies appears to be more relic than purposeful design: differential treatment of business and consumer debtors has never been a prominent feature of liquidation bankruptcy. For example, the Bankruptcy Act of 1800 does not even contemplate a difference between commercial entities and natural persons.² This is hardly surprising; in 1800, the concept of limited liability was still developing, and businesses were not meaningfully distinguished from their owners.³ The goal of Chapter 7 was straightforward: liquidate the debtor's assets

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1. For example, parties may request a trustee when the debtor-in-possession acts in bad faith. See 11 U.S.C. § 1104(a) (2018).
 2. See Act of Apr. 4, 1800, ch. 19, § 1, 2 Stat. 19, 20 (repealed 1803). The Bankruptcy Act of 1800 applied to “any merchant, or other person, residing within the United States, actually using the trade of merchandise,” treating a person’s trade as the person herself. *Id.* This was inherited from early English bankruptcy law, which applied only to “traders.” Charles Jordan Tabb, *The History of the Bankruptcy Laws in the United States*, 3 AM. BANKR. INST. L. REV. 5, 9 (1995).
 3. See Tabb, *supra* note 2, at 9 (noting that “the bankruptcy laws were viewed as a necessary concomitant to the exigencies of commerce, but no more,” with the implication that “[b]ankruptcy was limited to traders”); JONATHAN R. MACEY & DOUGLAS K. MOLL, *THE LAW OF BUSINESS ORGANIZATIONS: CASES, MATERIALS, AND PROBLEMS* 125 (14th ed. 2020) (outlining, in broad strokes, how corporate charters developed throughout the nineteenth and twentieth centuries). Justice Brandeis’s commentary on the changing nature of the corporation is also illuminating:

Through size, corporations, *once merely an efficient tool employed by individuals in the conduct of private business*, have become an institution The typical business corporation of the last century, owned by a small group of individuals, managed by their owners, and limited in size by their personal wealth, is being supplanted by huge concerns in which the lives of tens or hundreds of thousands of employees and the property of tens or hundreds of thousands of investors are subjected,

to compensate creditors. Whether the assets came from a corporation or a consumer was irrelevant; a sale was a sale.

Of course, the legal and economic backdrop for that uncomplicated notion of Chapter 7 has changed greatly since 1800.⁴ As corporations have become more complex, corporate law has developed into its own field. Chapter 7 trustees have changed their behavior accordingly; they (correctly) do not handle business and consumer liquidations in the same way. But Chapter 7 itself still fails to disentangle business and consumer liquidations, creating a system that is in tension not only with itself, but with bankruptcy law writ large. Indeed, the inefficiencies created by these tensions in Chapter 7 do not occur elsewhere in the Bankruptcy Code.

Consider the compensation of Chapter 7 trustees. Broadly speaking, the more debtor assets a trustee manages, the more compensation the trustee earns.⁵ Trustees administer assets in roughly 33% of corporate liquidations under Chapter 7. The assets in those cases are worth, on average, about \$986,855.⁶ By comparison, in 6% of consumer liquidations, trustees administer, on average, a trifling \$159,192.⁷ The other 94% do not involve unencumbered assets for which the trustee will be paid.⁸ Despite this enormous gap in assets, Chapter 7 dictates

through the corporate mechanism, to the control of a few men. Ownership has been separated from control

Louis K. Liggett Co. v. Lee, 288 U.S. 517, 565 (1933) (Brandeis, J., dissenting) (emphasis added).

4. See *Lee*, 288 U.S. at 565 (Brandeis, J., dissenting).
5. See 11 U.S.C. § 326(a) (2018).
6. These numbers were calculated from the Federal Judicial Center's (FJC) bankruptcy data. See *Integrated Database (IDB)*, FED. JUD. CTR. [hereinafter FJC Data], <https://www.fjc.gov/research/idb> [<https://perma.cc/GSC2-UMG3>]. Looking at the subset of cases closed under Chapter 7 that were filed between 2008 and September 2020, we calculated the percentage of business cases in which assets were distributed by dividing the total number of business (including LLC and LLP) Chapter 7 asset cases by the total number of business Chapter 7 cases. The asset values were calculated by taking the average of the total assets of business asset cases, trimmed at 1% to avoid outliers.
7. Similar to how we calculated the analogous figures for business cases, *see id.*, we calculated these figures using the FJC Data, *supra* note 6, evaluating the subset of cases closed under Chapter 7 that were filed between 2008 and September 2020. Here, the percentage of consumer cases in which assets were distributed was calculated by dividing the total number of consumer Chapter 7 asset cases by the total number of consumer Chapter 7 cases. The corresponding asset value was calculated by taking the average of the total assets of consumer asset cases, trimmed at 1% to avoid outliers.
8. *Id.*

that trustees be compensated for both business and consumer liquidations according to the same scheme.⁹

This entangled trustee-compensation scheme yields serious, unwelcome consequences. Most significantly, it makes Chapter 7 consumer cases extremely undesirable to trustees.¹⁰ In turn, this creates the risk of inequitable and inefficient system-wide outcomes. To cut costs, trustees may underinvestigate consumer cases, resulting in an unjust windfall for some debtors. Alternatively, trustees may overzealously investigate every consumer case they get to make those cases worth their while, subjecting those debtors to excessive takings.¹¹ The current scheme harms consumers seeking Chapter 7 protections even when there is no abnormal distortion of the ratio of business to consumer cases—in other words, even when times are normal.

But the COVID-19 pandemic has been anything but normal. As such, it has made Chapter 7's entanglement of business and consumer bankruptcies all the more relevant. The pandemic may precipitate abnormally high levels of consumer bankruptcy, reducing trustee compensation and incentivizing the aforementioned collection behaviors.¹² While large-business Chapter 11 bankruptcy filings (i.e., business cases involving over \$50 million in assets) nearly tripled between September 2019 and September 2020,¹³ total consumer-bankruptcy filings dropped by 28% in that same time frame.¹⁴ This decline is attributable to stopgap policies that halted collection on prepandemic consumer debt and extended cash support.¹⁵ In the second quarter of 2020 alone, there were approximately 281,000 fewer consumer cases than would have been expected from historical trends.¹⁶ But these policies did not eliminate that debt: given the nature

9. For example, 11 U.S.C. § 326(a) (2018) and 11 U.S.C.A. § 330 (West 2021) draw no distinction among Chapter 7 trustees.

10. For evidence of heterogeneity among trustees, see Edward R. Morrison, Belisa Pang & Jonathan Zytneck, *Manipulating Random Assignment: Evidence from Consumer Bankruptcies in the Nation's Largest Cities 22-24* (Columbia Univ. Ctr. for L. & Econ. Stud., Working Paper No. 614, rev. Sept. 18, 2021) (on file with authors).

11. *Cf. id.* at 33 fig.7 (demonstrating high variation between trustees with respect to the size of asset distribution to creditors, among other metrics).

12. *See infra* Section II.C.

13. Jialan Wang, Jeyul Yang, Benjamin Iverson & Raymond Kluender, *Bankruptcy and the COVID-19 Crisis* 3, 6 (Harvard Bus. Sch., Working Paper No. 21-041, 2020), https://www.hbs.edu/ris/Publication%20Files/21-041_a9e75f26-6e50-4eb7-84d8-89da3614a6f9.pdf [<https://perma.cc/7NDH-J82U>]; *see also id.* at 21 tbl.1 (providing summary statistics).

14. *Id.* at 21 tbl.1.

15. *Id.* at 2.

16. *See id.* at 3 (“If the historical relationship between the unemployment rate and consumer bankruptcy filings had continued, we would have expected to see over 200,000 additional

of the government’s policy of relief-by-deferral, it would stand to reason that most—if not all—of these would-be cases will materialize in the proximate future, when indebted consumers’ deferred payments become due.¹⁷ If and when those consumers do file, our novel empirical evidence from the analogous post-2008-financial-crisis bankruptcy boom strongly suggests that they will face undercompensated trustees determined to make up the shortfall in compensation by subjecting consumers to unfair levels of investigation.¹⁸

At the same time, the pandemic’s impact on American households and businesses has also brought significant legislative attention to bankruptcy issues.¹⁹ For example, while Congress for years consistently ignored pressures from practitioners and academics to raise trustee compensation,²⁰ it introduced and enacted the Bankruptcy Administration Improvement Act (BAIA) of 2020²¹ in less than five weeks.²² Yet this “fix” was arguably more of a condemnation of Chapter 7 than a vote of confidence: Congress chose to prop up Chapter 7’s entangled

consumer filings in the second quarter of 2020 relative to the second quarter of 2019. Instead, there were about 81,000 fewer consumer filings year-over-year in the second quarter.” (citing *id.* at 25 tbl.A1)).

17. See, e.g., Adam J. Levitin, Opinion, *Reform Our Bankruptcy Laws Before a Tsunami of COVID Debt Comes Due*, CNBC (Jan. 11, 2021, 9:04 AM EST), <https://www.cnbc.com/2021/01/11/op-ed-reform-bankruptcy-laws-before-covid-debt-comes-due.html> [<https://perma.cc/T534-XDMJ>] (“Collection moratoria merely stop collection actions; they do not cancel debts. . . . When the moratoria lapse, consumers will still owe months of back rent or mortgage payments, not to mention interest and late fees that have been accruing.”).
18. See *infra* Section II.B.
19. For recent legislative action on bankruptcy issues, see, for example, the COVID-19 Bankruptcy Relief Extension Act of 2021, Pub. L. No. 117-5, 135 Stat. 249, which extends COVID-19-related bankruptcy relief; the Consolidated Appropriations Act, 2021, H.R. 133, 116th Cong. § 1001 (2020) (enacted), which includes several temporary changes to the Bankruptcy Code in response to the COVID-19 pandemic; the Coronavirus Aid, Relief, and Economic Security Act (CARES Act), Pub. L. No. 116-136, § 1113, 134 Stat. 281, 310-12 (2020), which expands access to Subchapter V, 11 U.S.C. §§ 1181-1195 (2018), and allows modification to Chapter 13 plans; and the Bankruptcy Administration Improvement Act of 2020, Pub. L. No. 116-325, § 3, 134 Stat. 5086, 5087-89 (2021), which increases trustee compensation. See also Consumer Bankruptcy Reform Act of 2020, S. 4991, 116th Cong. (2020) (proposing a radical reform of consumer bankruptcy); Consumer Bankruptcy Reform Act of 2020, H.R. 8902, 116th Cong. (2020) (same).
20. Cf. Ariane Holtschlag, *ABI Consumer Commission: Chapter 7 Trustee Compensation (H.R. 3553)*, AM. BANKR. INST. J., Nov. 2018, at 8, 9 (“[T]he need to raise trustee compensation appears to enjoy almost unanimous support. Congress has not increased the \$60 fee for a no-asset case since 1994.”).
21. 134 Stat. 5086.
22. See *All Actions S.4996—116th Congress (2019-2020)*, CONGRESS.GOV, <https://www.congress.gov/bill/116th-congress/senate-bill/4996/all-actions> [<https://perma.cc/WUQ8-F4NJ>] (noting that the bill, introduced on December 9, 2020, became a public law on January 12, 2021).

scheme by subsidizing it with proceeds from Chapter 11's largely disentangled scheme.²³ It is clear, then, that the Act is not the end of the discussion. There is still a need and opportunity for intelligible reform of Chapter 7's monolithic approach to business and consumer liquidations. Congress's remarkable responsiveness to bankruptcy issues in the wake of the pandemic makes this a ripe moment to harmonize Chapter 7 with the rest of bankruptcy law by disentangling Chapter 7 trustees.

Other literature often discusses the difference between business and consumer bankruptcy (both liquidation and reorganization alike) by focusing on only one of the two.²⁴ While there is scholarship criticizing Chapter 7 on various grounds, little (if any) scholarship has identified a crucial source of the inefficiencies created by Chapter 7: its one-size-fits-all approach to the role of trustees in consumer and business liquidations. The gap in the literature has been revealed in large part by recent empirical papers that have demonstrated the distortions created by Chapter 7.²⁵ This Note is the first to leverage these fresh empirical insights to challenge Chapter 7's entangled regime directly, in favor of a disentangled one.

Part I of this Note provides necessary background on the role of trustees in Chapter 7. Section I.A briefly defines and compares consumer and business bankruptcy. Section I.B provides an institutional background on trustees' powers. Section I.C lays out the ways in which Chapter 7 governs these powers, focusing in particular on Chapter 7's sole differentiation between consumer and business bankruptcies and its trustee-assignment protocol. Part II marshals empirical evidence to elucidate the alarming distortions created by Chapter 7's failure to properly differentiate between business and consumer liquidations in its trustee-compensation scheme.

23. § 3(b), (c), 134 Stat. at 5087-89 (to be codified at 28 U.S.C. §§ 589a(f)(1)(C), 330(e) (2018), respectively).

24. See, e.g., Barry Adler, Ben Polak & Alan Schwartz, *Regulating Consumer Bankruptcy: A Theoretical Inquiry*, 29 J. LEGAL STUD. 585 (2000) (focusing on consumer bankruptcy); Alan Schwartz, *A Normative Theory of Business Bankruptcy*, 91 VA. L. REV. 1199 (2005) (focusing on business bankruptcy); William C. Whitford, *The Ideal of Individualized Justice: Consumer Bankruptcy as Consumer Protection, and Consumer Protection in Consumer Bankruptcy*, 68 AM. BANKR. L.J. 397 (1994) (focusing on consumer bankruptcy).

25. See, e.g., Morrison et al., *supra* note 10, at 33 fig.7 (detailing variation in decision-making among trustees); Samuel Antill, *Are Bankruptcy Professional Fees Excessively High?* 4 (rev. Aug. 18, 2021) (unpublished manuscript), <https://ssrn.com/abstract=3554835> [<https://perma.cc/282S-PYUF>] (performing analysis to "evaluate how trustee behavior and creditor recovery would change if the legally mandated trustee compensation scheme were to change"); Lois R. Lupica, *The Consumer Bankruptcy Fee Study: Final Report*, 20 AM. BANKR. INST. L. REV. 17, 95 (2012) (analyzing a survey to which "[h]undreds of chapter 7 panel trustees responded").

Part III then uses the evidence in Part II to present four normative arguments in favor of formally differentiating Chapter 7 trustees' roles with respect to business and consumer liquidations. First, consumers are fundamentally different from businesses, a powerful insight reflected throughout most of bankruptcy law. Second, from an economic perspective, the social benefit created by the trustee is different in consumer and business cases. Third, a trustee's work is different in consumer and business bankruptcies. Fourth, trustees interact differently with other parts of the judicial system depending on whether the debtor is a consumer or a business.

Part IV then proposes two realistic, actionable policy changes. First, consumer and bankruptcy cases should be managed by two different groups of trustees with different specializations. Second, trustees should receive more fixed compensation for consumer bankruptcy than for business cases. Part V concludes.

I. BACKGROUND: THE TRUSTEE'S ROLE IN BANKRUPTCY

A. Comparing Consumer and Business Bankruptcy

Before introducing a substantive discussion of Chapter 7, it will be instructive for this Note to clarify the scope of the terms "consumer bankruptcy" and "business bankruptcy." In the U.S. bankruptcy system, "[t]he term 'person' includes individual[s], partnership[s], and corporation[s], but," with a few exceptions, "does not include governmental unit[s]."²⁶ A person can hold consumer debt or business debt. The Bankruptcy Code defines "consumer debt" as "debt incurred by an individual primarily for a personal, family, or household purpose."²⁷ Under the case law of many jurisdictions, "[c]onsumer debt can also be differentiated from non-consumer debt because non-consumer debt is debt incurred with a motive for profit."²⁸

26. 11 U.S.C. § 101(41) (2018).

27. *Id.* § 101(8).

28. *In re Pollard*, 296 B.R. 531, 533 (Bankr. W.D. Okla. 2003) (citing *In re Stewart*, 175 F.3d 796, 806 (10th Cir. 1999)); *see also In re Johnson*, 546 B.R. 83, 101 n.16 (Bankr. S.D. Ohio 2016) (acknowledging and citing cases that apply the "profit motive" test); *In re Terzo*, 502 B.R. 553, 557 (Bankr. N.D. Ill. 2013) ("[Consumer debt] is to be contrasted with debt incurred for a business venture or with a profit motive." (citing *In re Sekendur*, 334 B.R. 609, 618 (Bankr. N.D. Ill. 2005)); *In re McElwee*, 469 B.R. 566, 583-84 (Bankr. M.D. Pa. 2012) (similar); *In re Vianese*, 192 B.R. 61, 67-68 (Bankr. N.D.N.Y. 1996) (similar); *In re Kelly*, 841 F.2d 908, 913 (9th Cir. 1988) (similar). In this Note, we use the words "business debt" and "nonconsumer debt" interchangeably.

In practice, the distinction between consumer debt and business debt matters only to a set of narrow, technical legal questions, the most important being whether the court can dismiss a case under section 707(b) of the Bankruptcy Code.²⁹ Outside of section 707(b), the formal distinction between consumer and business debt has little, if any, impact on the set of applicable laws, including rules related to the selection and supervision of trustees. Moreover, the categorization does not always intuitively relate to the nature of the debtor. For example, under the definition applicable to section 707(b), courts consistently hold that student loans are not per se consumer debt, which means that it is possible to categorize some student loans as business debt,³⁰ even though student loans are necessarily taken out by natural persons. So that it is clear, this Note uses the term “consumer bankruptcies” to refer to bankruptcies filed by individuals holding consumer debt. It uses the term “business bankruptcies” to refer to bankruptcies filed by nonindividuals holding nonconsumer debt.

There are three primary kinds of bankruptcy available to consumers or businesses: Chapter 7, Chapter 11, and Chapter 13.³¹ Chapter 7 is generally available

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29. 11 U.S.C. § 707(b) (2018). The distinction between business and consumer debt is central to the applicability of the so-called “means test” for eligibility for Chapter 7 bankruptcy, introduced by the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA). See Pub. L. No. 109-8, § 102(a)(2)(C), 119 Stat. 23, 27-32. Under the means test, a debtor whose disposable income is above the state median has to overcome additional hurdles to be eligible for Chapter 7 bankruptcy. See 11 U.S.C. § 707(b)(1)-(2) (2018). However, like the rest of section 707(b), this test applies only to a Chapter 7 debtor “whose debts are primarily consumer debts.” *Id.* § 707(b)(1). Therefore, individuals with relatively high incomes can argue that their debt is primarily business debt so that they can file for bankruptcy under Chapter 7. Additionally, prior to BAPCPA, “Section 707(b) provide[d] that upon its own motion, or that of the U.S. Trustee, a court may dismiss an individual Chapter 7 case if the debts involved are ‘primarily consumer debts’ and the court finds that granting relief would constitute a ‘substantial abuse’ of the provisions of Chapter 7.” *In re Vianese*, 192 B.R. at 67 (quoting 11 U.S.C. § 707(b) (1994)).
30. See, e.g., *In re Steiner*, No. 19-60062, 2020 WL 2027250, at *6 (Bankr. S.D. Ill. Jan. 29, 2020) (“Rather than adopting either a per se rule or the profit motive test, this Court believes that the appropriate way to determine whether a particular student loan constitutes consumer debt is to consider the totality of the circumstances on a case by case basis.” (emphasis omitted)); *In re Ferreira*, 549 B.R. 232, 237 (Bankr. E.D. Cal. 2016) (similar); *In re Rucker*, 454 B.R. 554, 558 (Bankr. M.D. Ga. 2011) (similar).
31. While there are other Chapters, such as Chapter 9 for municipalities and other similar entities, see 11 U.S.C. § 109(c) (2018), Chapter 12 for certain family farmers and fishermen, see *id.* § 109(f), and Chapter 15 for the recognition of foreign bankruptcies, see *id.* § 1501, these Chapters are reserved for their highly specific contexts. Therefore, they are outside the scope of this Note.

to both individuals and businesses;³² Chapter 11 is primarily used by businesses;³³ and Chapter 13 is reserved exclusively for “individual[s] with regular income” who owe debts above certain threshold amounts.³⁴ The primary difference between these three regimes is in how assets are administered, that is, what will happen to the assets and who will hold them. In Chapter 11, the debtor usually continues to operate the business as a “debtor in possession,”³⁵ but the appointment of a trustee may be required under section 1104 in certain circumstances, such as when the debtor is acting in bad faith.³⁶ In Chapter 13, a trustee is appointed to manage the estate,³⁷ but Chapter 13 debtors are allowed to keep their assets.³⁸ Instead of liquidating those assets, those debtors must surrender their disposable income for three to five years following a plan approved by the court.³⁹ In contrast, the Chapter 7 trustee is appointed to oversee the collection and liquidation of all assets,⁴⁰ except for assets exempted from bankruptcy under state and federal laws.⁴¹ While consumer debtors may avail themselves of either Chapter 7 or Chapter 13, the consumer debtors in Chapter 7 tend to be more vulnerable than their counterparts in Chapter 13. In particular, they tend to be

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32. Compare *id.* § 109(b) (establishing that, subject to certain conditions, “[a] person may be a debtor under chapter 7 of this title”), with *id.* § 101(41) (“The term ‘person’ includes individual[s], partnership[s], and corporation[s] . . .”).
33. See *id.* § 109(d); see also *Chapter 11—Bankruptcy Basics*, U.S. CTS., <https://www.uscourts.gov/services-forms/bankruptcy/bankruptcy-basics/chapter-11-bankruptcy-basics> [<https://perma.cc/3WJK-CS79>] (“This chapter [11] of the Bankruptcy Code generally provides for reorganization, usually involving a corporation or partnership.” (emphasis added)).
34. 11 U.S.C. § 109(e) (2018).
35. *Id.* § 1101(1); see also *id.* § 1107(a) (“[A] debtor in possession shall have all the rights . . . and powers, and shall perform all the functions and duties . . . of a trustee serving in a case under this chapter.”).
36. *Id.* § 1104(a).
37. See *id.* § 1302 (describing the appointment and duties of the Chapter 13 trustee).
38. *Id.* § 1306(b) (“Except as provided in a confirmed plan or order confirming a plan, the debtor shall remain in possession of all property of the estate.”); see also *Chapter 13—Bankruptcy Basics*, U.S. CTS., <https://www.uscourts.gov/services-forms/bankruptcy/bankruptcy-basics/Chapter-13-bankruptcy-basics> [<https://perma.cc/WVN8-4RV5>] (explaining the logistics of Chapter 13 proceedings).
39. 11 U.S.C.A. § 1325(b)(1)-(4) (West 2021).
40. *Id.* § 704(a)(1)-(12).
41. The *Butner* rule—named after the case that established it—states that “[a]part from [certain] provisions, . . . Congress has generally left the determination of property rights in the assets of a bankrupt’s estate to state law.” *Butner v. United States*, 440 U.S. 48, 54 (1979) (citing *Sturges v. Crowninshield*, 17 U.S. (4. Wheat.) 122 (1819); *Ogden v. Saunders*, 25 U.S. (12 Wheat.) 213 (1827)).

poorer than Chapter 13 debtors,⁴² and some data suggest that they are less likely to be employed.⁴³ They may also be more likely to experience negative mental-health outcomes due to the Chapter 7 process.⁴⁴

As both Chapter 11 and Chapter 13 allow the debtor to retain control over her assets, they are sometimes referred to as “reorganization bankruptcy.”⁴⁵ In contrast, because Chapter 7 aims to liquidate as many assets as permissible, it is usually referred to as “liquidation bankruptcy.”⁴⁶ As Chapters 11 and 13 are different Chapters of the Bankruptcy Code, Congress and the courts can implement changes to the treatment of business reorganizations that do not affect the treatment of consumer reorganizations, and vice versa. In contrast, Chapter 7 simultaneously governs both business and consumer liquidations. As a result, Chapter 7 is necessarily comprised of one-size-fits-all regulations. However, as the following Sections demonstrate, Chapter 7 trustees *in fact* treat business and consumer bankruptcies differently, creating tensions between the prescription and practice of Chapter 7.

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42. Between 2010 and September 2020, the median monthly income was about \$3,320 for Chapter 13 filers and \$2,500 for Chapter 7 filers, a 32.8% difference. These numbers were calculated by taking the median of the average monthly income for all consumer filers that were filed originally under Chapter 13 and Chapter 7. *See supra* notes 6-8; *cf.* Pamela Foohey, Robert M. Lawless & Deborah Thorne, *Portraits of Bankruptcy Filers*, 56 GA. L. REV. (forthcoming 2022) (manuscript at 32 tbl.4), <https://ssrn.com/abstract=3807592> [<https://perma.cc/KDD9-PYGS>] (listing median monthly incomes for Chapter 7 and Chapter 13 filers across a variety of household dimensions, with the median monthly income for all consumer Chapter 7 debtors being \$3,225 and the median monthly income for Chapter 13 filers being \$4,330).
43. *See* Foohey et al., *supra* note 42 (manuscript at 32 tbl.4). *But cf.* Jonathan D. Fisher, *Who Files for Personal Bankruptcy in the United States?*, 53 J. CONSUMER AFFS. 2003, 2010-11 (2019) (finding that, while Chapter 13 filers had slightly higher rates of employment, “[o]verall on income and employment, there is little difference between chapter 7 and chapter 13 filers”).
44. *See* Fenaba R. Addo, *Seeking Relief: Bankruptcy and Health Outcomes of Adult Women*, 3 SSM-POPULATION HEALTH 326, 331 (2017) (“Chapter 7 filers fared worse in terms of physical health relative to those who did not file and in depressive symptoms relative to Chapter 13 filers [T]he results suggest that there was something about the structure of Chapter 7 bankruptcy that is contributing to poorer health outcomes for these women.”).
45. *E.g.*, JAMES P. CAHER & JOHN M. CAHER, *PERSONAL BANKRUPTCY LAWS FOR DUMMIES* 19 (2d ed. 2006) (referring to Chapter 13 as “reorganization”); Arturo Bris, Ivo Welch & Ning Zhu, *The Costs of Bankruptcy: Chapter 7 Liquidation Versus Chapter 11 Reorganization*, 61 J. FIN. 1253, 1253 (2006) (referring to Chapter 11 as “reorganization”); *About the Program*, U.S. DEP’T JUST., <https://www.justice.gov/ust/about-program> [<https://perma.cc/DX9Q-B26K>] (referring to Chapter 11 as governing “reorganization proceedings” and to Chapter 13 as governing “[w]age-earner’ reorganization proceedings”).
46. *E.g.*, *About the Program*, *supra* note 45 (referring to Chapter 7 as governing “[l]iquidation proceedings”).

B. The Trustee's Duties and Powers in Chapter 7 Bankruptcy

In theory, Chapter 7 trustees should treat consumer liquidations the same as business liquidations. Section 323 of the Bankruptcy Code indicates that “the trustee . . . is the representative of the estate.”⁴⁷ For Chapter 7 specifically, section 704 of the Bankruptcy Code provides the same list of trustee duties for both consumer and business cases.⁴⁸ “[T]he bankruptcy trustee performs both adjudicatory and administrative functions.”⁴⁹ As an administrator of the estate, the trustee evaluates, collects, and liquidates the debtor’s assets for distribution to the creditors.⁵⁰ As a preliminary adjudicator, the trustee verifies the debtor’s financial documents and the creditors’ proofs of claims.⁵¹

Actual practice belies this ostensible mandate. Representation of the estate entails different work for businesses and consumers. A Chapter 7 trustee’s primary role in business bankruptcies is undoubtedly to pursue and sell assets.⁵² Unlike their consumer counterparts, a large proportion of Chapter 7 business bankruptcies have a significant amount of tangible and intangible assets for the trustee to collect and liquidate.⁵³ Trustees do not have a free hand in this liquidation process. As this Note demonstrates, they are kept in check by counsel for the debtor and the creditors, and they must regularly appear before judges both to justify their asset decisions and pursue claims within a more adversarial context.

47. 11 U.S.C. § 323(a) (2018).

48. *Id.* § 704.

49. *Curry v. Castillo (In re Castillo)*, 297 F.3d 940, 951 (9th Cir. 2002).

50. *See* 11 U.S.C. § 704(a)(1) (2018) (“[The trustee shall] 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.”).

51. *See id.* § 704(a)(4) (“[The trustee shall] investigate the financial affairs of the debtor.”); *id.* § 704(a)(5) (“[I]f a purpose would be served, [the trustee shall] examine proofs of claims and object to the allowance of any claim that is improper.”).

52. *E.g.*, Stephen J. Lubben, *Business Liquidation*, 81 AM. BANKR. L.J. 65, 68 (2007) (“While the Bankruptcy Code and its predecessors have long offered multiple avenues for terminating a business’s operations, chapter 7 is the tool that most people immediately think of upon any mention of bankruptcy. The theme in chapter 7 is the speedy collection, reduction to cash, and distribution of the debtor’s assets.”).

53. Among Chapter 7 cases filed between 2008 and September 2020, 33% of business cases had assets for distribution, compared to only 6% of consumer cases, and the average value of these businesses’ assets was close to \$1 million. *See supra* notes 6-8 and accompanying text.

In contrast, because most consumer cases do not involve assets to distribute,⁵⁴ trustees often need only administer paperwork and oversee meetings required by section 341.⁵⁵ But trustees nevertheless dominate the consumer-bankruptcy process: the trustee is often the only agent of the court with whom the debtor will ever interact;⁵⁶ rarely will a debtor see a judge, and there are virtually no jury trials in consumer bankruptcy.⁵⁷ As a result, many vital decisions are left substantially to the discretion of the trustee.⁵⁸ Trustees exercise power over consumer cases tantamount to that of a judge,⁵⁹ and they enjoy similar levels of immunity for their decisions.⁶⁰ For instance, a trustee can allow a debtor to keep

54. *Supra* notes 7-8 and accompanying text.

55. In most cases, the trustee investigates the debtor's financials through a "meeting of creditors," often called "341 meetings" or "341 hearings" because they are authorized by section 341 of the Bankruptcy Code, 11 U.S.C. § 341 (2018).

56. See, e.g., *In re Peterson*, 566 B.R. 179, 191 (Bankr. M.D. Tenn. 2017) ("Most debtors will never see anyone associated with the system and their case outside of the trustee The § 341 meeting and the trustee are their only direct interaction with the bankruptcy system.").

57. See Pamela Foohey, *A New Deal for Debtors: Providing Procedural Justice in Consumer Bankruptcy*, 60 B.C. L. REV. 2297, 2317 (2019) (discussing the lack of procedural justice in consumer bankruptcy).

58. For example, a trustee has wide discretion in the disposition of an asset under the "business judgment rule," which affords a trustee's decision a presumption of reasonableness even if that decision compromises the estate's claims. See *Paloian v. Greenfield (In re Rest. Dev. Grp., Inc.)*, 402 B.R. 282, 292 (Bankr. N.D. Ill. 2009) ("The business judgment rule protects bankruptcy trustees from mistakes in judgment where discretion is allowed."); *In re Batt*, 488 B.R. 341, 353 (Bankr. W.D. Ky. 2013) ("This Court is always reluctant to disregard the business judgment of the Trustee with respect to the settlement or compromise of the bankruptcy estate's claims, as it is that Trustee who is more knowledgeable of the strengths and weaknesses of their cases.").

59. For example, Judge Steven Rhodes points out that the trustee's "duties and powers are extraordinary, both in reality and appearance," and that "in the Chapter 7 process, the trustee is most often the only person that the parties actually observe exercising any of the authority of law." Steven Rhodes, *The Fiduciary and Institutional Obligations of a Chapter 7 Bankruptcy Trustee*, 80 AM. BANKR. L.J. 147, 152 (2006) (footnotes omitted). In his view, "many of the ethical obligations of a judge and a trustee overlap," *id.* at 153, such that "a trustee faced with an ethics issue should consider the ethical rules applicable to federal judges," *id.* at 153-54.

60. See, e.g., *Curry v. Castillo (In re Castillo)*, 297 F.3d 940, 950 (9th Cir. 2002) ("To the extent the trustee performed the functions of a modern-day bankruptcy judge, immunity would have extended to the performance of these common-law adjudicatory functions." (citing *Antoine v. Byers & Anderson, Inc.*, 508 U.S. 429, 433-34 & n.8 (1993))); *Gregory v. United States/U.S. Bankr. Ct. for Dist. of Colo.*, 942 F.2d 1498, 1500 n.1 (10th Cir. 1991) (noting that trustees enjoy "absolute quasijudicial immunity"); *Lonneker Farms, Inc. v. Klobucher*, 804 F.2d 1096, 1097 (9th Cir. 1986) ("[A trustee] is entitled to derived judicial immunity because he is performing an integral part of the judicial process." (citations omitted)); see also *Baron v. Sherman (In re Ondova Ltd.)*, 914 F.3d 990, 993 (5th Cir. 2019) ("[T]rustees have qualified immunity for personal harms caused by actions taken within the scope of their official duties."

certain assets by declining to investigate them or by formally “abandoning” them when they consider the value to be “inconsequential,”⁶¹ even if unsecured creditors are entitled to them.⁶² Conversely, the trustee can engage in rigorous investigation and delay the debtor’s discharge from bankruptcy.⁶³ In the Northern District of Illinois (NDIL), for example, with respect to asset collection, the most “aggressive” trustee collects assets from consumer debtors 19.9 times more often than her least aggressive peer, and certain trustees have a much higher chance of keeping consumer cases open past 120 days.⁶⁴ These unchecked “soft” powers give trustees much wider latitude in administering consumer cases than the letter of Chapter 7 might suggest.

There are two main reasons why section 704’s nondifferential treatment of business and consumer liquidation leads to significantly different work for trustees managing cases in each category. First, business bankruptcies tend to be

(citations omitted)); *Grant, Konvalinka & Harrison, PC v. Banks, Morgan, & Banks & Assoc. (In re McKenzie)*, 716 F.3d 404, 413 (6th Cir. 2013) (“A bankruptcy trustee is liable personally only for acts willfully and deliberately in violation of his fiduciary duties.” (quoting *Ford Motor Credit Co. v. Weaver*, 680 F.2d 451, 462 (6th Cir. 1982))). Additionally, when a debtor sues a trustee, she risks being sanctioned. *See, e.g., Woodruff v. Kelley (In re Woodruff)*, 610 B.R. 707, 713 (Bankr. M.D. Ga. 2019), *appeal dismissed on procedural grounds*, No. 7:19-CV-216, 2020 WL 4960592 (M.D. Ga. Aug. 24, 2020), *appeal docketed*, No. 20-13613 (11th Cir. Sept. 24, 2021) (granting a trustee’s motion for sanctions under Federal Rule of Bankruptcy Procedure 9011—a parallel to Federal Rule of Civil Procedure 11—because the court found that the debtor’s complaint against the trustee was frivolous).

61. *See* 11 U.S.C. § 554(a) (2018) (“After notice and a hearing, the trustee may abandon any property of the estate that is burdensome to the estate or that is of inconsequential value and benefit to the estate.”). “Abandonment is the ‘formal relinquishment of the property at issue from the bankruptcy estate.’” *In re Pena*, 600 B.R. 415, 422 (B.A.P. 9th Cir. 2019), *aff’d*, 974 F.3d 934 (9th Cir. 2020) (quoting *Catalano v. Comm’r*, 279 F.3d 682, 685 (9th Cir. 2002)). Trustees may also abandon an encumbered asset if it is worth little or less than the security interest, such that there is only “inconsequential value” to the estate. *See* 11 U.S.C. § 554(a) (2018). In that case, the debtor may still need to surrender the asset to the secured creditor outside of bankruptcy. *See* U.C.C. § 9-609(a) (AM. L. INST. & UNIF. L. COMM’N 2010).
62. The U.S. Trustee (UST) provides guidance to private trustees on how to determine whether to administer assets. This guidance allows the trustee to exclude assets from the estate if the trustee determines that they would not result in “meaningful” distributions, notwithstanding that unsecured creditors are nominally entitled to these distributions. *See* Exec. Off. for U.S. Trs., *Handbook for Chapter 7 Trustees*, U.S. DEP’T JUST. § 4(C)(3) (Oct. 1, 2012), https://www.justice.gov/ust/file/handbook_for_chapter_7_trustees.pdf/download [<https://perma.cc/6RHL-MSSV>].
63. Morrison et al., *supra* note 10, at 24 (finding that a subset of trustees—“disfavored trustees,” from the perspective of debtors’ attorneys—tend to “have relatively high case durations, are substantially more likely to file three or more motions per case and are much more likely to find assets that can be distributed to creditors, especially tax refunds”).
64. *Id.* at 33 fig.7.

much larger than consumer bankruptcies. Based on data from the Federal Judicial Center (FJC), an average corporation in bankruptcy holds \$380,482 of assets and \$1,462,285 of liabilities – a substantial part of which requires a trustee’s oversight.⁶⁵ Moreover, as previously mentioned, about 33% of business liquidation cases are asset cases – meaning that they have unencumbered assets that require the trustee’s administration – and the assets in these cases are worth \$986,855 on average.⁶⁶ In contrast, only 6% of consumer cases are asset cases, with an average consumer only holding \$89,454 of assets compared to \$155,934 in liabilities.⁶⁷ Consequently, consumer cases create far fewer asset-contingent jobs for trustees, and the fixed work that the trustees need to repeat for every consumer case – such as filing paperwork, collecting forms, and hosting 341 meetings – becomes much more important.

Second, nondebtor lawyers (mainly creditors’ counsel) participate in consumer bankruptcy at much lower rates than in business bankruptcy.⁶⁸ Participation of counsel shapes the bankruptcy process immensely. While the Bankruptcy Code describes trustees as “disinterested,”⁶⁹ many jurisdictions have determined that trustees have fiduciary duties to both the estate and the creditors, but not to the debtor.⁷⁰ Therefore, trustees are usually allowed to seek assets aggressively

65. These numbers are for cases filed between 2008 and September 2020, and all averages are obtained after trimming at 1%. Asset values were computed from total asset values reported in the FJC Data, while liability values were computed from the reported total liabilities values. See FJC Data, *supra* note 6.

66. *Id.*

67. See *supra* notes 7–8 and accompanying text.

68. For example, a prior study documented that only half of the creditors even bothered to send in proofs of claims. Dalíé Jiménez, *The Distribution of Assets in Consumer Chapter 7 Bankruptcy Cases*, 83 AM. BANKR. L.J. 795, 806–07 (2009). Creditors who do not send in proof of their claims cannot subsequently take action against the debtor, eliminating any possibility that their attorneys could participate in the bankruptcy. See FED. R. BANKR. P. 3002(a).

69. 11 U.S.C. § 701 (2018).

70. *E.g.*, *In re Morris Senior Living, LLC*, 504 B.R. 490, 491 (Bankr. N.D. Ill. 2014), *aff’d sub nom.* *Morris Healthcare & Rehabilitation Ctr., LLC v. Berish (In re Morris Senior Living, LLC)*, 526 B.R. 750 (N.D. Ill. 2014) (“A bankruptcy trustee owes fiduciary duties to the debtor’s estate and its creditors.” (citing *In re Chicago Art Glass, Inc.* 155 B.R. 180, 187 (Bankr. N.D. Ill. 1993))); *Wisdom v. Gugino (In re Wisdom)*, 490 B.R. 412, 417 (D. Idaho 2013), *aff’d*, 649 F. App’x 583 (9th Cir. 2016) (“[T]he trustee does not owe a fiduciary duty to the debtor. Rather, a Chapter 7 trustee is ‘the “legal representative” and “fiduciary” of the estate.’” (first citing *New Concept Housing, Inc. v. Poindexter (In re New Concept Housing, Inc.)*, 951 F.2d 932, 938 (8th Cir. 1991); and then quoting *Dye v. Brown (In re AFI Holding, Inc.)*, 530 F.3d 832, 844 (9th Cir. 2008))); *In re McCann, Inc.*, 318 B.R. 276, 287 (Bankr. S.D.N.Y. 2004) (“As a bankruptcy trustee, the plaintiff owes fiduciary duties to the estate and its creditors.” (citing *Pereira v. Foong (In re Ngan Gung Rest.)*, 254 B.R. 566, 570 (Bankr. S.D.N.Y. 2000)). Under the law of some jurisdictions, trustees do have a fiduciary duty to debtors when there are surplus

from the debtor regardless of the administrative burden on – or personal harm to – the debtor,⁷¹ even if the asset being collected would ordinarily be exempted under state law.⁷² In business bankruptcies, where the debtors and creditors are equally well-represented by a veritable army of bankruptcy lawyers, accountants, and professional managers, the trustees have much less leeway to act unilaterally.⁷³

In contrast, debtors in consumer bankruptcy are often unsophisticated and underrepresented. A significant minority of debtors appear pro se,⁷⁴ making errors that result in dismissal of their filings at much higher rates than represented debtors.⁷⁵ Even where debtors have counsel, it may be a sole lawyer to whom the

funds. See *Stoll v. Quintanar (In re Stoll)*, 252 B.R. 492, 495 n.4 (B.A.P. 9th Cir. 2000); *In re Kile*, 415 B.R. 723, 728 (Bankr. D. Ariz. 2009); *Nickless v. Kessler (In re Berman)*, 352 B.R. 533, 542 (Bankr. D. Mass. 2006); *United States ex rel. George Schumann Tire & Battery Co. v. Grant (In re George Schumann Tire & Battery Co.)*, 145 B.R. 104, 107 (Bankr. M.D. Fla. 1992). In consumer-bankruptcy cases, however, assets are often much less than liabilities, limiting the circumstances under which a fiduciary duty may be established. See *Ebel v. King (In re Ebel)*, 338 B.R. 862, 873-74 (Bankr. D. Colo. 2005) (determining that the trustee owed no fiduciary to the debtor where “[the] bankruptcy estate [was] hopelessly insolvent”).

71. Trustees’ immunity for harming the debtor when maximizing the value of the estate – thereby fulfilling their fiduciary duties to the creditors – applies equally in all Chapter 7 cases. For further explanation, see sources cited *supra* note 70.
72. For example, a trustee may liquidate an asset when the debtor erroneously claimed an exemption, even if other exemptions might apply. See *In re Wisdom*, 490 B.R. at 417.
73. Just as a trustee owes no fiduciary duty to the debtor, the lawyer for a Chapter 7 debtor owes no duties to the bankruptcy estate. See, e.g., *Peterson v. Sanches (In re Mack Indus., Ltd)*, 606 B.R. 313, 322 (Bankr. N.D. Ill. 2019) (“A chapter 7 debtor’s lawyer does not owe a duty of loyalty to the bankruptcy estate.”).
74. See, e.g., Foohey et al., *supra* note 42 (manuscript at 45 tbl.7) (indicating that 87% of Chapter 7 filers had an attorney, and another 6% had the assistance of a petition preparer, while the rest were categorized as pro se); Ed Flynn, *The Changing Profile of Chapter 7 Filers*, AM. BANKR. INST. J., Sept. 2018, at 36, 74 (“The percentage of chapter 7 cases filed pro se has increased in recent years. The pro se rate among joint filers has stayed fairly constant at around 4 percent each year. However, the pro se rate among solo filers has risen from about 7 percent to approximately 11 percent.”); Michael B. Joseph, *Consumer Pro Se Bankruptcy: Finding Hope in Hopelessness*, AM. BANKR. INST. J., May 2016, at 32, 32 (“[T]he number of pro se consumer bankruptcy case filings is considerable. During the year ending Dec. 31, 2015, there were a total of 49,344 chapter 7 pro se cases, or 9.2 percent of the national total, and 25,639 pro se chapter 13s, or 8.5 percent of the national total.”).
75. See, e.g., Rafael I. Pardo, *An Empirical Examination of Access to Chapter 7 Relief by Pro Se Debtors*, 26 EMORY BANKR. DEVS. J. 5, 23-31 (2009) (conducting empirical analysis and urging the reader to, “[i]f nothing else, consider that, among the study population’s post-BAPCPA dismissed cases involving pro se debtors, it is estimated that approximately 67.4% . . . of those cases were dismissed on the basis of failure to file information”); Foohey et al., *supra* note 42 (manuscript at 46 tbl.8) (noting that 34% of observed pro se Chapter 7 cases were dismissed, while only 4% of all consumer Chapter 7 cases were dismissed); Flynn, *supra* note 74, at 74

debtor must pay a fixed rate up front,⁷⁶ which can negatively affect the quality of representation. Consider the following excerpt:

[I]t is also not uncommon for bankruptcy trustees to report that at the § 341 hearing, they observe such problems for represented debtors as: i) attorneys not knowing the identity of their clients; ii) clients unprepared to testify; iii) ill-advised reaffirmation agreements; iv) debtors who will not be well-served by a bankruptcy case; v) budgets that are incomplete or not credible; or vi) schedules that predate the filing.⁷⁷

Creditors, for their part, are much less enthusiastic about their claims in Chapter 7 consumer cases. For example, empirical work has documented that in Chapter 7 cases with general unsecured claims, as many as half of all creditors do not even bother to send in proofs of claims.⁷⁸ The somewhat-ironically-named “meeting of creditors” is sometimes sparsely attended,⁷⁹ with anecdotal evidence suggesting that creditors frequently do not attend at all.⁸⁰ This lack of participation allows trustees to exert nearly unlimited influence over vital issues, such as the

(“Pro se chapter 7 debtors are nearly 10 times as likely to have their cases dismissed or their discharges denied than debtors with attorneys.”); *In re Hazlett*, No. BR 16-30360, 2019 WL 1567751, at *5 (Bankr. D. Utah Apr. 10, 2019) (“Not surprisingly, the Court’s statistics evidence that 30% of pro se Chapter 7 debtors fail to receive a discharge. . . . [P]ro se debtors can have their discharge denied under § 727, meaning instead of receiving a fresh start, they are shackled with a lifetime of nondischargeable debt.”).

76. See Tal Gross, Matthew J. Notowidigdo & Jialan Wang, *Liquidity Constraints and Consumer Bankruptcy: Evidence from Tax Rebates*, 96 REV. ECON. & STAT. 431, 435 (2014) (“[H]ouseholds that file under Chapter 13 are on average charged higher total legal fees but lower upfront fees, since legal fees can be written into the debtors’ repayment plans. Chapter 7 filers must typically pay all of their attorneys in advance of filing.”).
77. Michael D. Sousa, *Legitimizing Bankruptcy Petition Preparers: A Socio-Legal Prescription for Change* 13-14 (Univ. Denver Sturm Coll. L., Working Paper No. 15-04, 2015), <https://ssrn.com/abstract=2572501> [<https://perma.cc/FE5B-X5PG>].
78. See Jiménez, *supra* note 68, at 806 (“These five debtors scheduled a total of \$572,183 in general unsecured debt owed to 126 creditors, but all the claims in their cases only amounted to \$386,126 and only 63 creditors filed proof of claims, or half of the creditors.” (emphasis added)).
79. See *id.* at 806-07 (“It is also possible that repeat player creditors have such low expectations for recovery that they do not consider the process to be worth their time.”).
80. See, e.g., Cara O’Neill, *Will Creditors Show Up to My Meeting of Creditors?*, ALLLAW, <https://www.alllaw.com/articles/nolo/bankruptcy/will-creditors-show-up-meeting-of-creditors.html> [<https://perma.cc/F6HM-TGNK>] (“In most [consumer] cases, creditors rarely appear at the meeting of creditors.”); *The Chapter 7 “341(a) Meeting of Creditors”: What Should You Expect?*, PAOLUCCI L., <https://paoluccibankruptcy.com/chapter-7/chapter-7-341-meeting-of-creditors.html> [<https://perma.cc/EX92-XPBL>] (similar); *341 Meeting of Creditors During Bankruptcy—What to Expect*, LAW OFFS. KRETZER & VOLBERDING P.C. (Oct. 13, 2020, 7:00 AM), <https://kretzerfirm.com/341-meeting-of-creditors-during-bankruptcy-what-to-expect>

intensity of the investigation into the debtors' financial affairs and the abandonment of assets. Trustees can exert this influence based on their own convenience and business model without being checked by any adversarial proceeding.

C. *The Regulation of Trustees*

Given the outsized and vital role that trustees play in consumer bankruptcy, it is surprising that Chapter 7 governs both consumer and business cases with roughly the same rules. In all jurisdictions except for Alabama and North Carolina, Chapter 7 private trustees are assigned and supervised by one of the twenty-one regional U.S. Trustees (USTs), who act as “bankruptcy watchdogs” under the Department of Justice (DOJ).⁸¹ Private trustees receive written performance reviews at least every two years and are subject to occasional audits, field exams, and case-administration reviews by the USTs.⁸² Typically, each Judicial District has a panel of private trustees for each courthouse in the District.⁸³ Unlike

[<https://perma.cc/GV8S-9SGN>] (similar); *Chapter 7 Bankruptcy: What Happens at the Meeting of Creditors?*, LUCID L., <https://www.karinalucidlaw.com/chapter-7-bankruptcy-what-happens-at-the-meeting-of-creditors-in-newark-and-trenton-vicenages-in-new-jersey> [<https://perma.cc/N85E-AN2G>] (similar); *What Happens at a 341 Meeting of Creditors?*, ARM LAWS., <https://armlawyers.com/practice-areas/bankruptcy/what-happens-at-a-341-meeting-of-creditors> [<https://perma.cc/79F7-DRHT>] (similar).

81. H.R. REP. NO. 95-595, at 4 (1977); see *About the Program*, *supra* note 45. In Alabama and North Carolina, the role of the USTs is fulfilled by “Bankruptcy Administrators.” See U.S. GEN. ACCT. OFF., No. B-248877.1, BANKRUPTCY ADMINISTRATION: JUSTIFICATION LACKING FOR CONTINUING TWO PARALLEL PROGRAMS 4 (1992) (“In 1986, additional bankruptcy legislation expanded the UST program nationwide, with the exception of the six judicial districts in Alabama and North Carolina. Congress authorized those two states to delay their entry into the UST program until 1992, subsequently extending the date 10 years to 2002. For those two states, a separate, parallel program with objectives identical to those of the UST program was created—the [Bankruptcy Administrator] program.” (footnote omitted)).
82. See Exec. Off. for U.S. Trs., *supra* note 62, § 6(B)-(C). Practically, this oversight may be of limited effect. During the 2016 fiscal year (the most recent year for which data exist), the UST conducted 270 field exams and audits of private trustees. *Findings Most Likely to Result in an “Inadequate” Audit Opinion or Field Exam Conclusion and Their Frequency in FY 2014 to FY 2016 Chapter 7 Audits and Field Exams All Regions*, U.S. DEP’T JUST., https://www.justice.gov/ust/file/fy2014_2016_inadequate_likely_findings.pdf/download [<https://perma.cc/4BPR-XMFU>]. It found only seven trustees to be “inadequate.” *Id.* Private trustees were more frequently deemed “inadequate” for failure to adhere to internal controls than for the case-administration problems that are the subject of this Note. *Id.*
83. For example, the United States Bankruptcy Court for the Northern District of Illinois currently has thirty-four trustees in Cook County, and each trustee has her own preference for how to conduct the 341 meeting. *Cook County 341 Trustee Preferences*, U.S. BANKR. CT. FOR N.D. ILL., <https://www.ilnb.uscourts.gov/cook-county-341-trustee-preferences> [<https://perma.cc/V6JK-DFXU>].

judges, panel trustees are typically private lawyers rather than public employees.⁸⁴ These panel trustees often hold positions at large law firms or have their own practices, usually specializing in business bankruptcy.⁸⁵

The formal laws regulating trustees in business and consumer cases barely differ. For example, the rules governing trustees' appointment and qualifications are the same,⁸⁶ as are the laws governing trustees' compensation,⁸⁷ which professional trustees may retain at the expense of the estate,⁸⁸ and reimbursements of trustees' expenses.⁸⁹ Just as in the rest of Chapter 7, there are few, if any, rules that recognize the significant differences between consumer and business bankruptcy.⁹⁰

The only real difference between Chapter 7's rules for consumer and business bankruptcies is in the trustee-assignment protocol. In consumer bankruptcy, USTs utilize "a blind rotation system" that "normally results in asset cases being fairly and equally distributed among the panel [of trustees]" over time.⁹¹ The actual assignment protocol differs from region to region and is not always perfectly blind.⁹² The same panel of trustees also administers business-bankruptcy cases, and they are supervised by the same UST.⁹³ The difference is that trustees' assignment to business cases is not random. First, the USTs can pick specific trustees for business cases as "exceptions."⁹⁴ Second, trustees can resign from such cases if they do not want them.⁹⁵ Third, and perhaps most importantly, eligible general unsecured creditors can nominate a trustee pursuant to section

84. Lupica, *supra* note 25, at 95 (describing Chapter 7 trustees as "private professionals").

85. Morrison et al., *supra* note 10, at 5 ("The panel of trustees for the Northern District of Illinois, for example, includes 44 private attorneys, a substantial number of whom work at large law firms (e.g., Jenner & Block) or specialize in business bankruptcies in their own practices."); Lupica, *supra* note 25, at 95 ("Forty-six percent of respondents reported having a full-time chapter 7 trustee practice, and 54% reported a part-time practice.").

86. See 28 C.F.R. § 58.3 (2021).

87. See, e.g., 11 U.S.C. § 326(a) (2018) (drawing no distinction among Chapter 7 trustees).

88. See *id.* § 327.

89. See 11 U.S.C.A. § 330(a)(1)(B) (West 2021).

90. One rule that does recognize the difference is the exemptions rule. See 11 U.S.C. § 522(b) (2018) (allowing individual debtors—but not businesses—to exempt certain property from trustee collection).

91. Exec. Off. for U.S. Trs., *supra* note 62, § 2(F).

92. See Morrison et al., *supra* note 10, at 22-24 (detailing how attorney gamesmanship leads to trustee assignment becoming functionally nonrandom).

93. See Exec. Off. for U.S. Trs., *supra* note 62, § 2.

94. *Id.* § 2(F).

95. *Id.* § 2(J).

702 of the Bankruptcy Code to replace the interim trustee.⁹⁶ This nomination and the corresponding election take place at the 341 meeting with the interim trustee.⁹⁷

Without additional differentiation in the rest of Chapter 7, however, the different trustee-assignment protocols create more problems than they solve. As the current rule requires the same panel of trustees to administer both consumer and business cases, trustees often treat the administration of unprofitable consumer cases as a burden that must be endured to obtain lucrative business cases.⁹⁸ This incentivizes trustees to strategically manage their cases in a way that makes them attractive for consideration of future business cases.⁹⁹ As discussed above, they might do so by cutting costs on consumer cases—for example, by minimizing the time they spend investigating assets—so that they can prioritize business cases. Alternatively, trustees might vigorously pursue debtor assets to make the case worth their while. Since trustees are randomly assigned to consumer debtors, these debtors are effectively exposed to a lottery. As discussed in more detail below, the system thus fails to treat like cases alike.¹⁰⁰

II. DISTORTIONS CAUSED BY CHAPTER 7 TRUSTEE COMPENSATION

This Part examines a critical aspect of Chapter 7: the trustee-compensation scheme. While some studies persuasively argue that trustees are undercompensated,¹⁰¹ we argue that the root cause of Chapter 7’s problems is that consumer cases are treated the same way as business cases, even though their practical differences militate towards a different incentive structure. Section II.A describes the compensation scheme and the recent changes made by the 2020 BAIA. Section II.B summarizes recent empirical evidence demonstrating the undesirable

96. 11 U.S.C. § 702 (2018). See generally Richard C. Friedman, *A Guide to Trustee Elections*, U.S. DEP’T JUST. (1999), <https://www.justice.gov/archive/ust/articles/docs/trusteeelect02-00.pdf> [<https://perma.cc/75E8-UWU6>] (explaining the mechanics of trustee election).

97. Friedman, *supra* note 96, at 1.

98. Cf. Antill, *supra* note 25, at 3 (“The current law, which features \$60 debtor filing fees and high commissions, . . . forces creditors in asset cases to subsidize debtors in nonasset cases. Relative to nonasset cases, asset cases are roughly four times as likely to feature a business debtor. In this sense, corporate creditors subsidize unrelated individual debtors through Chapter 7 trustee compensation practices.” (footnote omitted)). To reframe Antill’s observation to focus on trustees rather than debtors, business bankruptcies subsidize trustees’ work on consumer bankruptcies.

99. See *infra* Section II.A.

100. See *infra* Section II.B.

101. See sources cited *infra* note 122.

consequences of the current regime. And Section II.C discusses these shortcomings in the context of both the COVID-19 crisis and the 2008 financial crisis.

A. Trustee Compensation in Chapter 7 Cases

Sections 326(a) and 330 of Title 11 govern the compensation to trustees in both consumer and business bankruptcies. Section 330 prescribes a minimum flat fee that the trustee usually receives regardless of the amount of assets she administers.¹⁰² This fee is not paid by the estate. Instead, it is taken from the debtor's filing fee, as well as from the Chapter 7 Trustee Fund.¹⁰³ The Chapter 7 Trustee Fund collects fees generated by cases commenced under other chapters of the Bankruptcy Code, such as from the Chapter 11 quarterly fee.¹⁰⁴ The 2020 BAIA expanded the flat fee authorized in section 330 by diverting funds away from Chapter 11.¹⁰⁵ While it is still unclear how the change will be implemented, the literal reading of the bill suggests that the flat fee can potentially be doubled to \$120 if the Chapter 7 Trustee Fund is sufficiently funded.¹⁰⁶ This additional payment is at least partially funded by additional fees collected from Chapter 11 cases,¹⁰⁷ which are mostly corporate. As over 94% of Chapter 7 consumer cases have no assets for distribution,¹⁰⁸ the Act effectively subsidizes these cases by using money collected from businesses filing for Chapter 11.

In addition to the flat fee, a trustee can also earn a variable fee that is capped at an amount tied to the value of the assets she distributes. In particular, section 326(a) prescribes a regressive system that caps a trustee's "reasonable compensation"¹⁰⁹ at no more than:

5 percent on the first \$5,000 or less, 10 percent on any amount in excess of \$5,000 but not in excess of \$50,000, 5 percent on any amount in excess

^{102.} See 11 U.S.C.A. § 330(b) (West 2021). This flat fee was \$60 until the Bankruptcy Administration Improvement Act (BAIA) of 2020 raised the fee, with trustees now getting paid \$60 plus the lesser of an additional \$60 or a specified payout from that portion of the UST System Fund stemming from Chapter 11 filings. See *id.* § 330(e).

^{103.} See *id.* § 330(b), (e); see also 28 U.S.C.A. § 589a(a) (West 2021) (establishing the fund).

^{104.} See 28 U.S.C.A. § 589a(f)(1) (West 2021) (governing how fees collected under Chapter 11 will be distributed).

^{105.} See Bankruptcy Administration Improvement Act of 2020, Pub. L. No. 116-325, § 3(e)(B)(i), 134 Stat. 5086, 5087-89 (2021) (adding 28 U.S.C. § 589a(f)(1)(C) (2018) and 11 U.S.C. § 330(e) (2018)).

^{106.} See 11 U.S.C.A. § 330(e)(3)-(5) (West 2021).

^{107.} 11 U.S.C. § 326(a) (2018).

^{108.} For the calculation of these percentages, see *supra* notes 7-8.

^{109.} 11 U.S.C.A. § 330(a)(1)(A) (West 2021).

of \$50,000 but not in excess of \$1,000,000, and reasonable compensation not to exceed 3 percent of such moneys in excess of \$1,000,000¹¹⁰

The same formula applies to both consumer and business cases. Before the 2020 BAlA increased flat fees, the variable fee accounted for a much larger proportion of trustees' income: "For example, during 2015 and 2016, . . . 15 percent [of Chapter 7 trustee compensation] came from the [flat fees], and 85 percent came from the percentage fee on distributions."¹¹¹

This seemingly standardized formula produces different results in consumer and business bankruptcy. In practice, most of the flat fees come from consumer bankruptcy, and most of the variable fees come from business bankruptcy.¹¹² In a 2015 response to a Freedom of Information Act (FOIA) request, the United States Trustee Program (USTP) disclosed the final reports of 2,411 business cases closed that year.¹¹³ The exact content of the FOIA request was not disclosed, but based on data from FJC,¹¹⁴ this list accounts for slightly more than a third of all business cases closed in 2015. Collectively, the listed business cases paid roughly \$48.6 million in total trustee compensation – about \$20,000 per case.¹¹⁵ However, the fixed fees authorized by section 330 – \$60 per case – only account for approximately \$144,660 of this amount.¹¹⁶ The variable fees, therefore, account for 99.7% of all trustee fees collected from these business asset cases.¹¹⁷

110. *Id.* § 326(a).

111. Holtschlag, *supra* note 20, at 71.

112. For flat fees, because the vast majority of cases are consumer cases and, by definition, the flat fee is the same for all cases, it follows logically that most flat fees come from consumer cases. As most consumer cases have no assets to distribute, they do not incur variable fees.

113. *Chapter 7 Trustee Final Report Data for Corporate Bankruptcies*, U.S. DEP'T JUST. (2015) [hereinafter 2015 FOIA Data], https://www.justice.gov/ust/file/ch7_2015_foia.xlsx/download [<https://perma.cc/YJK8-JNMP>]. It seems that the 2015 FOIA Data was created by supplementing information to a subset of business asset cases reported in a broader dataset. See U.S. Tr. Program, *Chapter 7 Trustee Final Reports*, U.S. DEP'T JUST. [hereinafter USTP Data], <https://www.justice.gov/ust/bankruptcy-data-statistics/chapter-7-trustee-final-reports> [<https://perma.cc/78C4-HHLN>].

114. FJC reports that, on the national level, there were 6,530 business Chapter 7 asset cases closed in calendar year 2015. See FJC Data, *supra* note 6. Therefore, the 2,411 asset cases reported in the 2015 FOIA Data cover roughly 37% of all business asset cases closed that year.

115. This number was calculated by dividing the sum of total trustee compensation of all listed cases by the total number of cases on the list. See 2015 FOIA Data, *supra* note 113.

116. This number was calculated by multiplying the total number of cases on the list by \$60. See *id.*

117. This number is 1 minus the proportion of total trustee compensation that comes from flat fees; this latter proportion was calculated by dividing \$144,660 by \$48.6 million.

In contrast, consumer bankruptcy contributes most of the flat fees. Because over 96% of Chapter 7 cases were filed by consumers¹¹⁸ and flat fees are definitionally the same for every case, consumers have contributed roughly 96% of all flat fees.¹¹⁹ If the abovementioned list of business cases from the U.S. Trustee Program data (USTP Data) is excluded, the average trustee fee drops to a mere \$2,376 per asset case¹²⁰ – barely more than a tenth of the average among business cases on the list. As only a third of the business bankruptcy cases were covered by the list, the actual average among consumer cases can only be lower. Moreover, because only about 6% of consumer cases are asset cases,¹²¹ in most cases the statutory flat fee as prescribed by section 330 is the only compensation to trustees, which is hardly enough to cover their costs.¹²²

As expected, trustees that are profit-seeking¹²³ agree to administer consumer cases usually because they expect to be assigned a profitable business case down the road.¹²⁴ Because consumer cases are barely profitable, the current compensation scheme incentivizes trustees to either cut the cost of managing consumer

118. We counted the total number of Chapter 7 cases listed as consumer by FJC and divided that number by the total number of Chapter 7 cases included in the FJC Data. So that it is clear, we excluded consumers with business debt from the total number of FJC consumer cases used to compute this percentage.

119. While some Chapter 7 filers are granted fee waivers because they cannot afford to pay, fewer than 5% were granted such waivers on an annual basis from 2007-2016, Holtschlag, *supra* note 20, at 8, so their effect on this number is likely trivial.

120. To get this number, we first calculated the sum of trustee compensation for all cases closed in 2015 listed in the U.S. Trustee Program data (USTP Data). USTP Data, *supra* note 113. Then, we subtracted trustee compensation for cases included in the 2015 FOIA Data, *supra* note 113. Finally, we calculated the average trustee compensation among the remaining cases. USTP Data, *supra* note 113.

121. For the calculation of these percentages, see *supra* notes 7-8.

122. See, e.g., Ed Flynn, *Chapter 7 Asset Cases and Trustee Compensation*, AM. BANKR. INST. J., June 2014, at 48, 92 (“[I]t is clear that [Chapter 7 trustees’] compensation has not kept up with the amount of work that is expected of them.”). Compare Holtschlag, *supra* note 20, at 71 (“Increasing compensation in the asset cases would improve overall trustee compensation and offset the losses [that] trustees will continue to suffer in the no-asset cases, even with a fee increase.”), with Flynn, *supra*, at 92 (recommending a trustee-fee increase that “would increase annual trustee compensation in the aggregate by an estimated \$36.1 million”).

123. Trustees who do not administer bankruptcies for profit are not strictly within the scope of this piece. It nevertheless merits noting that they are paid in the same way as other trustees. Accordingly, they might still be incentivized to spend less time on consumer cases.

124. Trustees seem to be rational actors who take the compensation scheme into account. For example, Robert C. Furr stated on behalf of the National Association of Bankruptcy Trustees that “[t]rustees essentially work on a ‘contingent’ basis because if their efforts do not result in a dividend to creditors, they receive only the \$60 no asset fee.” *Bankruptcy Trustee Compensation: Hearing Before the Subcomm. on Com. & Admin. L. of the H. Comm. on the Judiciary*, 110th

cases by underinvestigating and hastily disposing of them or aggressively overinvestigate consumer debtors' financial affairs to find sufficient assets to break even.¹²⁵

To complete the trustee-compensation puzzle, it is worth noting that trustees can employ their own law firms under section 327 at the expense of the estate.¹²⁶ Trustees may do so equally in consumer and business cases.¹²⁷ However, a study by Dalié Jiménez shows that professional fees were almost twice the size of trustee fees and expenses for consumer-bankruptcy asset cases.¹²⁸ Although the study did not investigate whether those professional fees *all* went to the trustees' own firms, it is likely that at least some of those fees did. While it is reasonable to expect that the hiring of professionals would cost a larger proportion of the estate's value in consumer cases than in business cases, more empirical studies are needed to draw that conclusion.

B. Distortions Caused by an Undifferentiated Compensation Scheme

As trustees derive more profits from business cases under the current compensation scheme, their administration of consumer cases can be distorted in ways that produce inequitable or inefficient outcomes. In particular, the welding of different assignment protocols onto Chapter 7's otherwise undifferentiated compensation scheme incentivizes Chapter 7 trustees to do one of two things. As discussed above,¹²⁹ these trustees can either (1) underinvestigate a consumer case in order to dispose of it quickly and potentially get a business case instead, or (2) ruthlessly seek assets from consumer debtors to make a consumer case worth their time.

This analysis is borne out by empirical evidence recently collected and analyzed by Edward R. Morrison, Belisa Pang (one of the coauthors of this Note),

Cong. 8 (2008) [hereinafter *Trustee Hearings*] (statement of Robert C. Furr, Founding Partner, Furr & Cohen, P.A.); *see also* Antill, *supra* note 25, at 3 (arguing that the distribution of asset cases interacts with the trustee-compensation rules to create a system in which "corporate creditors subsidize unrelated individual debtors through Chapter 7 trustee compensation practices").

125. *See infra* Section II.B. For data on the variation in collection behaviors, *see* Morrison et al., *supra* note 10, at 33 fig.7.

126. 11 U.S.C. § 327(a) (2018).

127. *See id.*

128. *See* Jiménez, *supra* note 68, at 802 fig.1, 803 (reporting that trustee fees equal 14.6% of assets recovered and professional fees equal 28.3%).

129. *See supra* Section II.A.

and Jonathon Zytznick¹³⁰ from the bankruptcy courts for the Central District of California (CDCA), Eastern District of New York (EDNY), NDIL, and the Southern District of Ohio (SDOH).¹³¹ These four districts cover over 1.5 million cases drawn from several important metropolises across different regions of the country where bankruptcy is relatively commonplace. Collectively, these cases represent about 15% of all consumer-bankruptcy cases filed in the United States between 2008 and September 2020, including about 13% of all Chapter 13 cases and 16% of all consumer Chapter 7 cases.¹³² Although this dataset does not include information from every bankruptcy court across the country, it is the largest dataset presently available that provides individual identifiers for trustees. Moreover, taken in conjunction with the national data undergirding all other empirical findings in this Note, the high level of heterogeneity present in each of these diverse districts suggests that these results are nationally generalizable.¹³³

The purpose of a trustee's investigation is to find assets for distribution. Therefore, the percentage of cases where the trustee ends up distributing assets (the "distribution rate") should be strongly correlated with the intensity of investigation. In other words, if the trustee audits more cases, there should be more discovery of hidden assets and, consequently, more distribution to unsecured creditors. Historically, the national average distribution rate for Chapter 7 consumer cases is about 6%, which means that trustees around the country do not find any nonexempt assets in over 94% of cases.¹³⁴

If trustees investigated all cases with the same intensity and all cases were randomly assigned, then we would expect similar distribution rates across the trustees. In reality, this does not occur. As Figure 1 shows, the historic distribution rate varies drastically across trustees. In NDIL, for example, the most "aggressive" trustee collects assets 19.9 times more often than his least aggressive

130. Morrison et al., *supra* note 10; *see, e.g., id.* at 33 fig.7 (demonstrating highly variable behaviors across trustees in the Northern District of Illinois (NDIL)).

131. Most of the results on trustee heterogeneity (as opposed to the broader issue of commingling that is the principal focus of this Note) come from Morrison et al., *supra* note 10. The raw dataset of that project contains cases filed between 2008 and 2017, and it includes 755,408 cases from the Central District of California, 145,366 cases from the Eastern District of New York, 468,513 cases from NDIL, and 216,094 cases from the Southern District of Ohio. Raw Dataset, PUB. ACCESS TO CT. ELEC. RECS. [hereinafter PACER Data] (on file with authors).

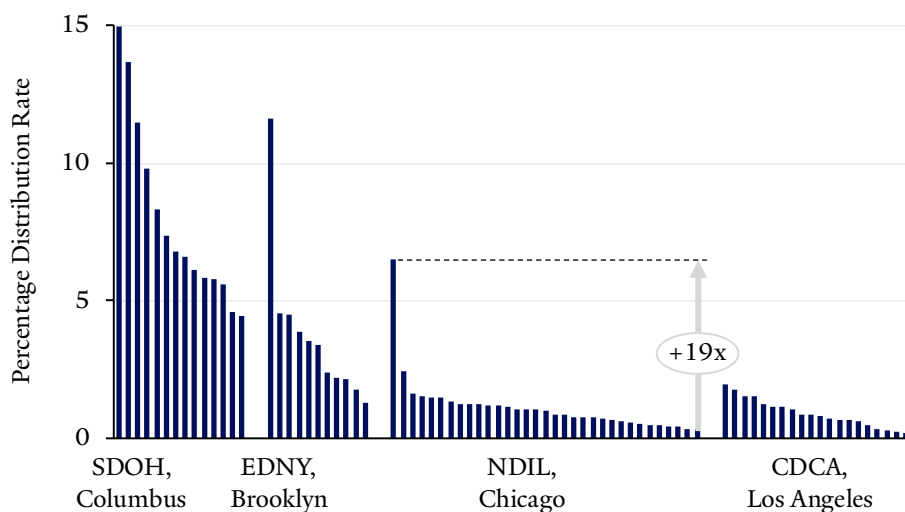
132. These percentages were calculated by dividing the number of cases in the four districts by the total number of cases reported by FJC, subset on consumer cases, consumer Chapter 7 cases, or consumer Chapter 13 cases filed between 2008 and September 2020. *See* FJC Data, *supra* note 6.

133. This analysis of heterogeneity is the only empirical finding in this Note not drawn from a national sample.

134. For the calculation of these percentages, *see supra* notes 7-8.

peer.¹³⁵ While the former found assets for distribution in about 6% of the cases, the latter found almost none.¹³⁶ The other three districts were not much different.

FIGURE 1. VARIATION IN DECISION-MAKING ACROSS TRUSTEES, DISTRIBUTION RATE BY TRUSTEE¹³⁷



Trustees who underinvestigate consumer cases per the first causal mechanism above make the system less fair and efficient. To dispose of a consumer case more swiftly, trustees might, for example, simply choose not to collect assets when the nonexempt value is small.¹³⁸ In NDIL, empirical evidence suggests that over 90% of tax refunds that should be collected for distribution are effectively

¹³⁵. We calculated this number by dividing the percentage of Trustee 18's Chapter 7 asset cases by the corresponding percentage of Trustee 22. We read these percentages from Figure 7(a) of Morrison et al., *supra* note 10, at 33 (reprinted here as Figure 1(d)).

¹³⁶. *Id.*

¹³⁷. According to the authors of Morrison et al., *supra* note 10, this graph excludes trustees with less than 100 cases from the sample, as well as a number of other special cases. All other cases from the PACER Data, *supra* note 131, were used to construct this Figure. The y-axis unit is percentage.

¹³⁸. For example, the trustee may choose to abandon an encumbered asset under 11 U.S.C. § 554(a) (2018).

ignored.¹³⁹ Furthermore, in *all* of the analyzed offices, some trustees' asset-case rates (i.e., the proportion of cases that have distributable assets) were a small fraction of the office average.¹⁴⁰ For these trustees, the work is effectively reduced to the administration of paperwork and the hosting of symbolic section 341 meetings.

These findings are alarming. Intuitively, the bankruptcy system should not hire trustees that will not investigate debtors' financial affairs. Moreover, when their behavior is taken in the aggregate, trustees who underinvestigate consumer cases to gain quicker access to business cases end up leaving behind a significant amount of money. A rough estimate based on the USTP Data on Chapter 7 suggests that the average consumer asset case generated approximately \$2,325 in distribution to general unsecured creditors in 2018.¹⁴¹ This is comparable to a study conducted a decade ago, which reported that trustees capture \$3,416 per consumer asset case on average.¹⁴² There is also a significant amount of related fees.¹⁴³ Trustees who underinvestigate consumer cases might leave this money on the table.

Moreover, trustee underinvestigation of consumer cases means that one debtor might unfairly experience a major windfall where her peers do not. This

139. This number was calculated based on results from Morrison et al., *supra* note 10, at 32, which reports that an "aggressive" trustee collected tax refunds in 4% of his cases. To get this number, we first calculated 4% times the total number of cases. Then, we subtracted the total number of cases where the tax refund was collected. Finally, we divided the second number by the first to obtain the percentage, which is slightly over 90%. Because Trustee 18 could have missed some tax refunds but cannot capture a refund when there is none, it is highly likely that the actual number is larger than 90%. Indeed, if one assumes that the underlying asset distribution of each trustee's caseload is identical, then the number must be larger than 90%. Even without that assumption, in a world where debtors have incentives to funnel cases away from aggressive trustees, *see id.* at 12, 90% still likely represents an underestimation.

140. *See supra* Figure 1.

141. To obtain this number, we took the following approach: because businesses tend to have more assets than consumers and business cases comprise roughly 13% of all asset cases closed in 2018, we ranked all asset cases by gross receipt and excluded the top 13%. We then ranked the remaining cases by distribution to general unsecured creditors and dropped the top 5% to remove outliers. Finally, we computed the average across all cases. Without dropping the top 5%, the average distribution to general unsecured creditors is \$3,253. *See* USTP Data, *supra* note 113. This is a rough estimate because the USTP Data do not distinguish consumer cases from business cases. To obtain the 13% number from the FJC Data, *supra* note 6, we used the number of business asset cases closed in 2018 under Chapter 7 as the numerator and the number of all asset cases closed in 2018 under Chapter 7 as the denominator.

142. Jiménez, *supra* note 68, at 797.

143. *Cf.* Antill, *supra* note 25, at 9 ("Across all Chapter 7 asset cases, [whether business or consumer,] the median sale value is equal to \$4,400. In roughly 75% of cases, the sale value is less than \$10,000 The trustee receives 22% of the sale value in the median case. In 75% of cases, the trustee receives at least 14% of the sale value.").

in turn creates an incentive for debtors to hide assets from trustees.¹⁴⁴ If trustees do not catch the underreporting, debtors will usually be able to keep the entire difference between the reported value of their assets and the actual value of those assets. This further encourages debtors to conceal assets, in turn making it more costly to audit the debtors because there are more assets for the trustee to look for. The result is a vicious cycle that enriches the dishonest at the expense of the honest. To be sure, intentional misrepresentation of assets can constitute a federal crime punishable by a fine or up to five years in prison.¹⁴⁵ The court can also deny the debtor's discharge if "the debtor, with intent to hinder, delay, or defraud" the trustee, "transferred, removed, destroyed, mutilated, or concealed" property.¹⁴⁶ But debtors are rarely caught and almost never punished¹⁴⁷ for misrepresenting assets. Additionally, for these legal remedies to apply in the first place, a prosecutor, the trustee, or the creditors must expose the fraud, which means that somebody must litigate the claims in court. When the cost of litigation exceeds the benefit—already meager in consumer cases—few rational parties would likely take such action.

At the opposite end of the spectrum are trustees who relentlessly seek consumer debtor assets in accordance with the second outlined causal mechanism. These trustees create extra work for debtors' attorneys,¹⁴⁸ who usually charge a fixed fee at the beginning of the case. When trustees frequently adjourn meetings and demand more work, debtors' attorneys respond by taking advantage of loopholes in the assignment protocols to avoid these trustees. Empirical evidence suggests that "[t]rustee-shopping is sufficiently pervasive in Chicago that it changes the identity of the trustee in about ten percent of cases."¹⁴⁹ There, the protocols assign cases in "batches," which means that several sequentially filed

144. For example, Nathaniel Pattison and Richard M. Hynes's recent paper shows that debtors systematically underreport the value of their homes to discourage trustees from pursuing their assets. Nathaniel Pattison & Richard M. Hynes, *Asset Exemptions and Consumer Bankruptcies: Evidence from Individual Filings*, 63 J.L. & ECON. 557, 591 (2020).

145. See, e.g., 18 U.S.C. § 152 (2018) (concealment of assets, false oaths and claims, and bribery); *id.* § 157 (bankruptcy fraud).

146. 11 U.S.C. § 727(a)(2) (2018).

147. For example, the Executive Office for United States Trustees reported in 2017 that it made 2,158 bankruptcy and bankruptcy-related criminal referrals in fiscal year 2016. Formal criminal charges were filed in connection with only sixteen referrals. The rest were closed, were not prosecuted, or remained under review. EXEC. OFF. FOR U.S. TRS., REPORT TO CONGRESS: CRIMINAL REFERRALS BY THE UNITED STATES TRUSTEE PROGRAM FISCAL YEAR 2016, at 3, 5 (2017).

148. Morrison et al., *supra* note 10, at 24 (finding that trustees disfavored by attorneys tend to "have relatively high case durations" and are "substantially more likely to file three or more motions per case").

149. *Id.* at 2.

cases will be assigned to the same trustee.¹⁵⁰ Additionally, some trustees do not receive cases on certain days due to scheduling reasons that are known to experienced attorneys.¹⁵¹ By filing cases strategically, experienced debtors' attorneys can minimize or neutralize the likelihood of being assigned to a disfavored trustee. This gamesmanship typically benefits the clients of these experienced attorneys at the expense of other debtors.

There is certainly no reason that Chapter 7 *should* work this way. The problems of underinvestigation and overinvestigation can be effectively addressed by differentially compensating trustees for consumer and business cases. In business cases, the variable component of the fee structure is crucial in incentivizing trustees to look for assets, while the \$60 flat fee serves no meaningful purpose.¹⁵² In contrast, in consumer cases, the expected contingent fee is often too small to justify the cost of rigorous investigation because the total amount of assets per case is typically small. Therefore, a more effective means to compensate the trustees is to guide – if not explicitly require – them to investigate consumers' financial affairs, while simultaneously providing them a sufficiently large flat fee to cover the fixed component of the trustees' expenses. The current scheme tries to accommodate two different types of bankruptcies. It ends up failing to properly accommodate either.

C. *The Impending Breakdown: COVID-19 and Lessons from 2008*

Chapter 7's commingling of business and consumer bankruptcies deserves special attention in light of the ways in which COVID-19 has impacted and will impact the system. The pandemic has had two principal effects with respect to Chapter 7. First, it has made Congress quite responsive to the need for Chapter 7 reforms, especially with respect to trustee compensation.¹⁵³ To be clear, Congress's Chapter 7 reforms to date do not resolve Chapter 7's entanglement of business and consumer liquidations. Nevertheless, they indicate that Congress has been sensitive to pandemic-driven issues in the bankruptcy system. Second, the pandemic may imminently precipitate an enormous number of consumer

150. *Id.* at 4.

151. *See id.* at 18–20. The knowledge of experienced attorneys could even extend beyond the routine practicalities of the assignment system. For example, an experienced attorney might know that a difficult trustee has an upcoming vacation and schedule her client's hearing during the vacation to avoid the trustee. In so doing, the attorney might improve her client's overall outcome.

152. *See, e.g., Trustee Hearings, supra* note 124, at 8 (statement of Robert C. Furr, Founding Partner, Furr & Cohen, P.A.) (“Trustees essentially work on a ‘contingent’ basis because if their efforts do not result in a dividend to creditors, they receive only the \$60 no asset fee.”).

153. For recent congressional action on bankruptcy issues, see sources cited *supra* note 19.

Chapter 7 filings, severely unbalancing the system and driving inequitable and inefficient collection behaviors.

It is difficult to overstate the degree to which the pandemic has heightened legislative attention to bankruptcy. Indeed, Congress has demonstrated an unprecedented enthusiasm for bankruptcy reforms since the pandemic began. Since 1994, Congress had resisted calls from bankruptcy academics and practitioners to reform Chapter 7 compensation.¹⁵⁴ Congress passed the Bankruptcy Abuse Prevention and Consumer Protection Act in 2005,¹⁵⁵ but that law functioned primarily to discourage consumers from availing themselves of Chapter 7 and left its fundamental business/consumer tensions untouched.¹⁵⁶ Years of external pressure and momentum eventually impelled the introduction of the 2017 BAIA,¹⁵⁷ but the bill stalled and was quickly abandoned.¹⁵⁸ In contrast, the 2020 Act of the same name – with similar but further-reaching content – was introduced on December 9, 2020¹⁵⁹ and became law on January 12, 2021.¹⁶⁰ The pandemic had, in other words, pushed Congress to accomplish greater Chapter 7 reforms in five weeks than it had in twenty-six years.

However, even the Chapter 7 reforms Congress implemented in the 2020 BAIA highlight the practical unworkability of Chapter 7’s commingling of business and consumer liquidations. One of the goals of the Act is to “provide[] long-

154. See Holtschlag, *supra* note 20, at 9 (noting that “Congress has not increased the \$60 fee for a no-asset case since 1994,” even though “the need to raise trustee compensation appears to enjoy almost unanimous support”).

155. Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8, 119 Stat. 23.

156. See, e.g., Tal Gross, Raymond Kluender, Feng Liu, Matthew J. Notowidigdo & Jialan Wang, *The Economic Consequences of Bankruptcy Reform* 1 (Nat’l Bureau of Econ. Rsch., Working Paper No. 26254, 2019), https://www.nber.org/system/files/working_papers/w26254/w26254.pdf [<https://perma.cc/MUV6-WUDV>] (“[BAPCPA] implemented a number of provisions that collectively made filing for bankruptcy more onerous, more expensive, and less financially beneficial.”); Robert M. Lawless, Angela K. Littwin, Katherine M. Porter, John A.E. Pottow, Deborah K. Thorne & Elizabeth Warren, *Did Bankruptcy Reform Fail? An Empirical Study of Consumer Debtors*, 82 AM. BANKR. L.J. 349, 349-53 (2008) (noting the reductions in bankruptcy filings since BAPCPA’s passage). Since BAPCPA, debtors who want to file for Chapter 7 bankruptcy must pass a “means test” which requires that their average monthly income be lower than the state median. Otherwise, a “presumption of abuse” will arise. 11 U.S.C. § 707(b)(2), (7) (2018).

157. Bankruptcy Administration Improvement Act of 2017, H.R. 3553, 115th Cong. (2017).

158. See *All Actions: H.R. 3553 – 115th Congress (2017-2018)*, CONGRESS.GOV, <https://www.congress.gov/bill/115th-congress/house-bill/3553/all-actions> [<https://perma.cc/M86V-SS2T>].

159. Bankruptcy Administration Improvement Act of 2020, S. 4996, 116th Cong. (as engrossed in Senate, Dec. 9, 2020).

160. Bankruptcy Administration Improvement Act of 2020, Pub. L. No. 116-325, 134 Stat. 5086 (2021).

overdue additional compensation for chapter 7 case trustees,”¹⁶¹ while “ensur[ing] that the bankruptcy system remains self-supporting.”¹⁶² It did so by expanding the Chapter 7 Trustee Fund, part of which will be used to give Chapter 7 trustees a pay raise capped at \$60 per case.¹⁶³ This potentially¹⁶⁴ doubles the fees that a Chapter 7 trustee can earn from the nonasset cases¹⁶⁵ that make up about 94% of consumer Chapter 7 cases. Curiously, however, the Act affected this fee raise partially by using money raised from Chapter 11 corporate restructurings. In other words, the Act attempts to fix the underfunding of a system that *entangles* business and consumer bankruptcy with money collected from a system that *disentangles* them, casting yet further doubt on the viability of the current configuration of Chapter 7. That said, the present reforms should not be regarded as uniformly negative. If nothing else, Congress’s sensitivity to the pandemic suggests that further reforms will be forthcoming should the pandemic continue to exacerbate the inherent tension of Chapter 7.

Unfortunately, there is ample reason to believe that the pandemic will do just that. It has already induced a wave of business bankruptcies,¹⁶⁶ and, in the proximate future, may induce an even greater wave of consumer bankruptcies.¹⁶⁷ Although the sheer number of possibly impending bankruptcies is certainly a cause

161. *Id.* § 2(a)(4), 134 Stat. at 5086.

162. *Id.* § 2(a)(2), 134 Stat. at 5086.

163. *See* 11 U.S.C.A. § 330(e) (West 2021).

164. The Director of the Administrative Office of the United States Courts promulgated interim regulations outlining the contours of this pay raise, which went into effect on September 30, 2021. *See* Regulations for the Administration of Payments to Chapter 7 Trustees Under Section 330(e) of the Bankruptcy Code, 86 Fed. Reg. 49,287 (Sept. 2, 2021).

165. The additional fee “shall be the lesser of— (A) \$60; or (B) a pro rata share, for each chapter 7 case, of the fees collected under section 1930(a)(6) of title 28 and deposited to the United States Trustee System Fund under section 589a(f)(1)(A) and (B) of title 28 [after certain deductions].” 11 U.S.C.A. § 330(e)(4) (West 2021). The 2020 BAIAs also added section 330(e)(5), which makes clear that the new pay raise will be added to the \$60 already granted to trustees under 18 U.S.C. § 330(b) (2018). Thus, if the pro rata amount to be paid from the fund would equal \$60, trustees could double their pre-2020 BAIAs base compensation.

166. *See, e.g.,* Wang et al., *supra* note 13, at 3-4 (“Thus far, the COVID-19 crisis has coincided with a wave of large corporate filings largely driven by sectors such as retail that were already struggling prior to the pandemic.”). FJC reports that, on the national level, 8,147 corporations, LLPs, and LLCs filed for bankruptcy between January and September 2020, compared to 6,940 that filed between January and September 2019—a 17% year-over-year increase. *See* FJC Data, *supra* note 6.

167. *See* Levitin, *supra* note 17; Mary Williams Walsh, *A Tidal Wave of Bankruptcies Is Coming*, N.Y. TIMES (Aug. 3, 2020), <https://www.nytimes.com/2020/06/18/business/corporate-bankruptcy-coronavirus.html> [<https://perma.cc/6CGL-2CWZ>]; Paige Marta Skiba, Dalié Jiménez, Michelle McKinnon Miller, Pamela Foohey & Sara Sternberg Greene, *Bankruptcy Courts Ill-Prepared for Tsunami of People Going Broke from Coronavirus Shutdown*, CONVERSATION (May

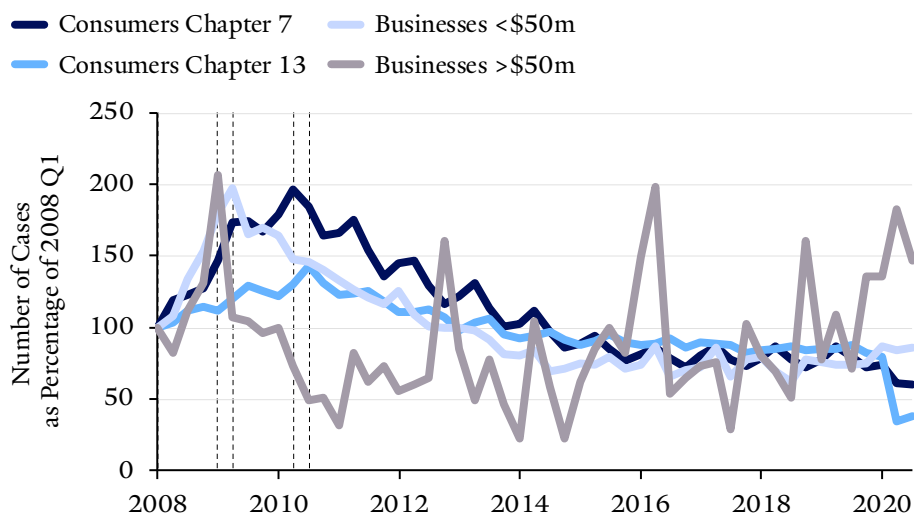
for concern, it is the likely the *timing* of these waves that poses the greatest threat to Chapter 7 in its current configuration. The present approach to trustee regulation essentially ties trustee compensation to the expectation that there will be a balanced mix of business and consumer cases. As detailed above, trustees receive just enough business cases to compensate them for the costs of handling large numbers of unprofitable consumer cases. However, when there are major economic crises, business and consumer cases tend to come in desynchronized waves – as they have in the wake of the present pandemic.¹⁶⁸ These desynchronized waves accentuate the structural problems in Chapter 7 caused by its comingling of business and consumer bankruptcy, incentivizing trustee collection behaviors that subvert the aims of the system and are manifestly unfair to consumers. Unless Congress implements reforms, this all but guarantees inequitable outcomes for consumers.

To illustrate the stakes, this Note performs a novel empirical analysis of the effect of the 2008 financial crisis on Chapter 7 filings. Figure 2 below shows the normalized total number of bankruptcy filings by debtor type.¹⁶⁹ In this Figure, we recorded cases by their filing date. The dotted lines mark the peak for each group. In both 2008 and 2020, large businesses reacted quickly to economic instability, filing for bankruptcy right away. Large business filings in response to the 2008 crisis peaked in early 2009, with smaller business filings following close behind. In contrast, the wave of consumer bankruptcies did not arrive until early 2010, when the bankruptcy filing rate for large businesses had already returned to precrisis levels. The percentage of post-2008 consumer filings remained relatively elevated until around 2016.

13, 2020, 8:38 AM EDT), <https://theconversation.com/bankruptcy-courts-ill-prepared-for-tsunami-of-people-going-broke-from-coronavirus-shutdown-137571> [https://perma.cc/8SQ6-46YG].

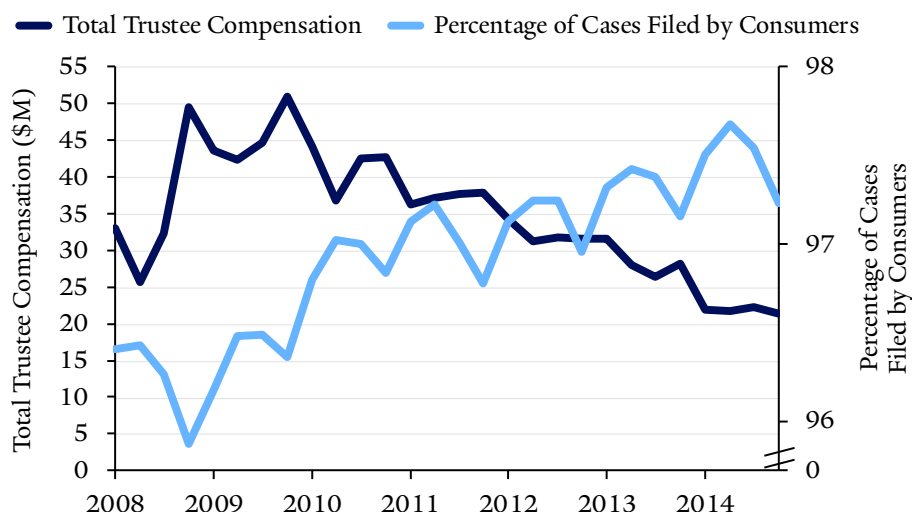
168. See *infra* Figure 2.

169. To make the plot, we drew on the FJC Data, *supra* note 6. We started by counting the number of cases in each category: consumer cases under Chapter 7 and Chapter 13, business cases with total assets under \$50 million, and business cases with total assets above \$50 million. Then, we normalized the numbers by dividing all numbers by the 2008 number of the corresponding category. Therefore, the y-axis shows the total number of cases as a percentage of the number of cases filed in 2008 for each category. Finally, we plotted the number against the fiscal quarters on the x-axis.

FIGURE 2. BANKRUPTCY FILING BY DEBTOR TYPE (NORMALIZED)

Chapter 7's commingling of business and consumer cases caused trustee compensation to fluctuate significantly during and after the 2008 financial crisis. As Figure 3 shows, Chapter 7 trustees' total compensation at the peak of business filings was 30% higher than their compensation at the peak of consumer filings a year later.¹⁷⁰ The lesson of 2008 therefore seems to be that when consumer filings disproportionately increase, trustee compensation decreases. When trustee compensation decreases, trustees become more incentivized to engage in undesirable collection behaviors, as described in Section II.B.

170. To make the plots, we first estimated the filing dates based on the closing month and days of each case. Then, we calculated the sum of total trustee compensation for cases approximately filed in each quarter between 2008 and 2015. Finally, we plotted the sum against the quarters, which are shown on the x-axis. USTP Data, *supra* note 113.

FIGURE 3. RELATIONSHIP BETWEEN TOTAL CHAPTER 7 TRUSTEE COMPENSATION AND PERCENTAGE OF CONSUMER CHAPTER 7 FILINGS

National data from the first three quarters of 2020 suggest that the nation may imminently experience the same phenomenon from the COVID-19 pandemic, but that the imbalance will be even more pronounced. A wave of businesses filed for bankruptcy in 2020, “and the [Chapter 11] filings with greater than \$50 million in assets have increased by nearly 200 percent.”¹⁷¹ Consumer-bankruptcy filings had a relatively steady decline in 2020, though they dropped precipitously at the onset of the pandemic.¹⁷² Much of that decline is the product of policies that halted collection on prepandemic consumer debt and extended cash support.¹⁷³ The number of consumer bankruptcies also remained low because of the practical difficulties of filing created by court shutdowns and quarantine orders.¹⁷⁴ However, the short-term relief policies did not *eliminate* consumer debt. It is possible that an enormous wave of consumer bankruptcy will unfold in the immediate future, probably within the next few years. Assuming conservatively that the same number of consumers would have filed for bankruptcy in 2020 as in 2019, approximately 208,000 consumer cases have been

171. Wang et al., *supra* note 13, at 3.

172. *Id.* (“While consumer Chapter 7 filings initially declined by 34 percent year-over-year from March 15th to April 30th, they began rebounding in mid-April and have stabilized around a 20 to 30 percent year-over-year decline from May through August.”).

173. See Levitin, *supra* note 17.

174. See Skiba et al., *supra* note 167.

postponed to the imminent future.¹⁷⁵ Another estimate suggests that 281,000 consumer cases were missing from the second quarter of 2020.¹⁷⁶ While academics and practitioners disagree on the timing and the magnitude of the wave, the consensus seems to be that consumer bankruptcy will rise in the coming years.¹⁷⁷ Accordingly, the pandemic will likely bring about a decrease in trustee compensation and a concomitant increase in undesirable, distortive collection behaviors on an even larger scale than in the aftermath of the 2008 financial crisis.

The burden of these unfair collection behaviors may fall on those already disproportionately disadvantaged by the pandemic. This pandemic has been most damaging to traditionally underprivileged groups, which were already more likely to end up in bankruptcy even before the current crisis.¹⁷⁸ Nearly 7.9 million of the 9.6 million net job losses from 2019 to 2020 occurred in the lowest 25% of wage earners, more than three times what would have occurred had losses

175. To obtain this number, we first counted the total number of consumer cases filed between January and September 2019 and the total number of consumer cases filed between January and September 2020. (The FJC Data we have run through September 2020. *Supra* note 6.) The difference between the two is how many cases that were “missing” in the first three quarters of 2020. Then, we estimated the number of cases that would be missing in the last quarter of 2020 by assuming that the proportion of missing cases stays the same. Finally, we added the actual number of the first three quarters to the estimated number of the last quarter. This is a relatively conservative estimation because it assumes that the number of bankruptcies will stay the same between years, even though, intuitively, the economic crisis should have caused more people to file for bankruptcy in 2020 than 2019.

176. *Supra* note 16 and accompanying text.

177. See Mark Henricks & Daphne Foreman, *After The Covid-19 Deluge, A Bankruptcy Tidal Wave?*, FORBES (Sept. 23, 2020, 9:16 AM EDT), <https://www.forbes.com/sites/advisor/2020/09/23/after-the-covid-19-deluge-a-bankruptcy-tidal-wave> [<https://perma.cc/FM8D-Q9EW>] (“[One expert] has little doubt that the not-too-distant future will feature more bankruptcy filings than we’ve seen in a long time, if not ever. . . . [Another expert’s] view of the prospects of a bankruptcy boom is more circumspect, but still somewhat short of outright optimism.”); Laurence Darmiento, *Bankruptcies Are Way Down During the Pandemic. Here’s Why*, L.A. TIMES (Mar. 23, 2021, 6:00 AM PT), <https://www.latimes.com/business/story/2021-03-23/covid-19-bankruptcies-pandemic> [<https://perma.cc/8W2S-3ZZ2>] (“[One expert] expects bankruptcies will rise and credit problems will emerge once the moratoriums are lifted and the government support is depleted.”); Andrew Keshner, *Bankruptcy Filings Fell in 2021, but Post-COVID “Shadow Debt” May Spell Trouble*, MARKETWATCH (June 19, 2021, 10:20 AM ET), <https://www.marketwatch.com/story/bankruptcy-filings-fell-in-2021-but-will-post-covid-shadow-debt-spell-trouble-for-americans-11623781507> [<https://perma.cc/6LGL-BE4L>] (similar); Soma Biswas & Harriet Torry, *Coronavirus Was Supposed to Drive Bankruptcies Higher. The Opposite Happened.*, WALL ST. J. (Mar. 29, 2021, 5:30 AM ET), <https://www.wsj.com/articles/coronavirus-was-supposed-to-drive-bankruptcies-higher-the-opposite-happened-11617010201> [<https://perma.cc/J3LB-CRJK>] (similar).

178. See Foohey et al., *supra* note 42 (manuscript at 32 tbl.4) (showing that less than half of all Chapter 7 debtors in the relevant sample had bachelor’s degrees); cf. A. Mechele Dickerson, *Race Matters in Bankruptcy*, 61 WASH. & LEE L. REV. 1725, 1771 (2004) (concluding that “the [Bankruptcy] Code systematically favors white debtors” over minority debtors).

been evenly distributed by income.¹⁷⁹ Arguably, the pandemic has affected low-income workers more seriously than even the 2008 financial crisis.¹⁸⁰ Similarly, Black and Hispanic adults, especially women, were among the most likely to report employment difficulties and trouble paying their bills, rents, and mortgages.¹⁸¹ People in these demographics similarly had the highest incidence of reporting that they had to dip into their savings and retirement accounts since the start of the pandemic.¹⁸² The marginalized – jeopardized not only by job loss, but also immobility and lack of access to childcare – may be disproportionately thrust into bankruptcy.¹⁸³ The magnitude of job loss and income reduction has

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179. Elise Gould & Jori Kandra, *The State of Working America 2020 Wages Report*, ECON. POL'Y INST. 7 (Feb. 24, 2021), <https://files.epi.org/pdf/219418.pdf> [<https://perma.cc/8YFA-TJTQ>]. Moreover, in case there was any ambiguity, the top quarter of wage earners gained 981,000 jobs. *Id.* at 8; see also Tomaz Cajner, Leland D. Crane, Ryan A. Decker, John Grigsby, Adrian Hamins-Puertolas, Erik Hurst, Christopher Kurz & Ahu Yildirmaz, *The U.S. Labor Market During the Beginning of the Pandemic Recession* 10-16 (Nat'l Bureau of Econ. Rsch., Working Paper No. 27159, 2020), https://www.nber.org/system/files/working_papers/w27159/w27159.pdf [<https://perma.cc/NN28-N6UY>] (showing considerable employment losses for workers in the lowest wage quintiles).
180. See Cajner et al., *supra* note 179, at 16, 24 (“The extent of nominal wage cuts and wage freezes are large relative to non-recessionary years and are even larger than what was observed in the Great Recession.”); see also Heather Long, Andrew Van Dam, Alyssa Fowers & Leslie Shapiro, *The Covid-19 Recession Is the Most Unequal in Modern U.S. History*, WASH. POST (Sept. 30, 2020), <https://www.washingtonpost.com/graphics/2020/business/coronavirus-recession-equality> [<https://perma.cc/HC5Q-UFC3>] (showing the disproportionate impact of the pandemic recession on low-wage and minority workers).
181. See Kim Parker, Rachel Minkin & Jesse Bennett, *Economic Fallout from COVID-19 Continues to Hit Lower-Income Americans the Hardest*, PEW RSCH. CTR. 9 tbl. (Sept. 24, 2020), https://www.pewresearch.org/social-trends/wp-content/uploads/sites/3/2020/09/SDT_2020.09.24_COVID-19-Personal-Finances_FINAL.update2.pdf [<https://perma.cc/BUU6-LK5N>] (displaying responses indicating that Black and Hispanic people have had more difficulty paying bills and mortgages since the onset of the virus); see also Titan Alon, Sena Coskun, Matthias Doepke, David Koll & Michèle Tertilt, *From Mancession to Shecession: Women's Employment in Regular and Pandemic Recessions* 60 (Nat'l Bureau of Econ. Rsch., Working Paper No. 28632, 2021), https://www.nber.org/system/files/working_papers/w28632/w28632.pdf [<https://perma.cc/RF24-KM6A>] (“[I]n a large set of countries, the Covid-19 recession had a much larger impact on women’s relative employment compared to pre-pandemic recessions.”).
182. Parker et al., *supra* note 181, at 11 tbl.
183. See Edward R. Morrison, Belisa Pang & Antoine Uettwiller, *Race and Bankruptcy: Explaining Racial Disparities in Consumer Bankruptcy*, 63 J.L. & ECON. 269, 269-73 (2020); Elizabeth Warren, *What Is a Women's Issue? Bankruptcy, Commercial Law, and Other Gender-Neutral Topics*, 25 HARV. WOMEN'S L.J. 19, 19-24 (2002); see also Geoff Smith & Sarah Duda, *Bridging the Gap II: Examining Trends and Patterns of Personal Bankruptcy in Cook County's Communities of Color*, WOODSTOCK INST. 8 & fig.3 (2011), https://woodstockinst.org/wp-content/uploads/2013/05/bridgingthegapII_may2011_smithduda.pdf [<https://perma.cc/BJ6J-NB2T>] (reporting

sown the seeds for the desynchronized wave of Chapter 7 consumer filers predicted above. It is difficult to imagine that these peoples' circumstances – made more acute by the pandemic – will be adequately accounted for in Chapter 7's entangled system.

Finally, it is worth emphasizing that the pandemic has not *produced* these problems in Chapter 7. The pandemic, like any major economic crisis, simply exacerbates the problems inherent to Chapter 7's commingled model. As such, it can act as a catalyst for legislative change. The form of those changes will, of course, be driven by the normative values of the entity making the change.

III. WHY DISTINGUISH CONSUMER TRUSTEES FROM BUSINESS TRUSTEES?

Building off Part II's empirical evidence, this Part presents four normative arguments for why consumer- and business-bankruptcy trustees should be regulated differently.

A. *Human Beings Fundamentally Differ from Corporations*

The dichotomy between the human nature of consumer debtors on the one hand and the artificial nature of business debtors on the other has become a signal feature of American bankruptcy law. Protection for individual debtors is, and has been, one of the most important differences between modern American bankruptcy law and its eighteenth-century English origins.¹⁸⁴ In recognizing the suffering of individual debtors, the colonies gradually erased the capital punishment imposed by England's 1705 Bankrupts Act¹⁸⁵ and instituted new laws that protected essential properties such as clothes and household goods.¹⁸⁶ By the early 1900s, the protection of individual debtors became recognized as a goal of

that, in Cook County, Illinois, 5.1 out of 100 women in predominately Black communities filed for bankruptcy between 2006 and 2010, as compared to 3.4 out of 100 men in those same communities during the same time frame).

184. Cf. Tabb, *supra* note 2, at 7 (“Early English law had a distinctly pro-creditor orientation, and was noteworthy for its harsh treatment of defaulting debtors.”).
185. Bankrupts Act 1705, 4 & 5 Ann. c. 17, § 1 (repealed) (specifying a procedure to be followed in the event of bankruptcy, and authorizing capital punishment as the penalty for noncompliance).
186. See, e.g., *id.* § 8 (authorizing capital punishment for bankruptcy fraud); BARRY E. ADLER, ANTHONY J. CASEY & EDWARD R. MORRISON, BAIRD & JACKSON'S BANKRUPTCY: CASES, PROBLEMS, AND MATERIALS 25 (5th ed. 2020) (describing the history of American bankruptcy and how providing a “fresh start” became the goal of individual bankruptcy); Tabb, *supra* note 2, at 9 (describing the history of American bankruptcy).

bankruptcy.¹⁸⁷ Moreover, as Louis Edward Levinthal observed, the bankruptcy law developed such that “execution for debt came to be directed against the property of the debtor rather than his person.”¹⁸⁸ The “chief desideratum” of the system then became compensation instead of personal retaliation.¹⁸⁹

The commingling of consumer and business liquidation bankruptcy in Chapter 7 is best regarded as a living fossil of English legal yore. As discussed in the Introduction, this commingling appears to stem from the fact that businesses were at one time regarded as not meaningfully different from the individual merchants running them. Execution against the former necessarily entailed execution against the latter. But this living fossil long outlived its time. The notion that “a sale is a sale” and that uniform rules will suffice for both natural and artificial people elides the crucial human element of consumer bankruptcy vindicated by Congress and the judiciary over the decades. From the debtor’s perspective, the human cost of foreclosing a home that shelters three children is necessarily different from the cost of, say, selling off a business’s patents. Similarly, adjourning a 341 meeting in a business case is most likely harmless, but repeatedly requiring a nurse who works long double shifts to come to the trustee’s office during business hours can cost her a job.¹⁹⁰

Barry Adler has written that, while “most of the scholarship on business bankruptcy has taken an ex post focus, concentrating on what should be done after a firm has become insolvent[,] . . . [t]here is no similar ex post efficiency paradigm for consumer bankruptcy.”¹⁹¹ In contrast, consumer-bankruptcy theories recognize individuals’ “nonwaivable right to bankruptcy relief and a choice

187. See Louis Edward Levinthal, *The Early History of Bankruptcy Law*, 66 U. PA. L. REV. 223, 224-25 n.11 (1919) (“In . . . America, the liberation of the honest insolvent from antecedent liability is an important element of bankruptcy.” (internal citation omitted)). *But cf. id.* at 225 (“[T]he protection of the honest debtor from his creditors, by means of the discharge, is sought and attained in some of the systems of bankruptcy, but this is by no means a fundamental feature of the law.”).

188. *Id.* at 232.

189. *Id.*

190. In fact, one of the major changes proposed by Senators Elizabeth Warren (D-MA), Dick Durbin (D-IL), and Sheldon Whitehouse (D-RI) and Representatives Jerrold Nadler (D-NY) and David Cicilline (D-RI) in the Consumer Bankruptcy Reform Act of 2020 (CBRA) was to waive the requirement for an in-person meeting “if it would impose an unreasonable burden on the debtor.” Consumer Bankruptcy Reform Act of 2020, S. 4991, 116th Cong. §§ 309(p)(3), 341(f)(2)(A) (2020); Consumer Bankruptcy Reform Act of 2020, H.R. 8902, 116th Cong. §§ 309(p)(3), 341(f)(2)(A) (2020). In turn, that bill provided for a rebuttable presumption of an unreasonable burden if the location is more than ten miles away from the home address indicated on the debtor’s bankruptcy petition. S. 4991 §§ 309(p)(3), 341(f)(2)(B); H.R. 8902 §§ 309(p)(3), 341(f)(2)(B). The attention this issue received shows that it is not merely a classroom hypothetical.

191. Adler et al., *supra* note 24, at 586.

as to the form that relief can take.”¹⁹² As we have argued, Chapter 7 is in tension both with itself and with broader bankruptcy law because it ignores these important theoretical differences. Even though the *Butner* rule defers the question of property rights to state law,¹⁹³ trustees have ample discretion over which assets to pursue in consumer bankruptcy and can thus largely dictate the outcome of a case.¹⁹⁴ Entangling consumer bankruptcy with business bankruptcy risks obscuring the human nature of consumers behind a bevy of considerations more appropriate for artificial persons. Keeping a business bankruptcy open for months to capture business assets for the benefit of creditors might be worthwhile from a societal perspective, but keeping a consumer bankruptcy open for months to capture tax refunds that the debtor might need for medical care might not be.

B. Trustees Create Different Socioeconomic Benefits in Business and Consumer Cases

Basic economic intuition dictates that trustee work, insofar as it reinforces creditor rights, can create positive externalities for society by lowering interest rates. If creditors can recover more assets in bankruptcy, it becomes less risky to make loans.¹⁹⁵ As a result, creditors are willing to lend at a lower interest rate and more debtors will be able to borrow.¹⁹⁶ The validity of this mechanism is supported by evidence on trustee discovery of distributable assets: historically,

192. *Id.* at 587; cf. ADLER ET AL., *supra* note 186, at 21-22 (stating that the purposes of bankruptcy include avoiding a destructive race to assets and protecting individual debtors).

193. *Butner v. United States*, 440 U.S. 48, 54-55 (1979) (“Congress has generally left the determination of property rights in the assets of a bankrupt’s estate to state law.”). For example, in Illinois, most debtors can exempt up to \$15,000 in homestead equity, *see* 735 ILL. COMP. STAT. 5/12-901(a) (2021), \$2,400 in one car, *id.* 5/12-1001(c), \$4,000 in “any other property” exemption, *id.* 5/12-1001(b), which is often referred to as the “wild card” exemption, *see, e.g., Galvin v. Bank of Am., N.A.*, No. 18 C 200, 2018 WL 6649554, at *1 (N.D. Ill. Dec. 19, 2018), and so on.

194. *Supra* notes 58-63 and accompanying text.

195. Ample literature in finance studies this relationship between asset collection, risk, and interest rate. *See, e.g.,* Gregory R. Duffee, *Estimating the Price of Default Risk*, 12 REV. FIN. STUD. 197 (1999); Robert C. Merton, *On the Pricing of Corporate Debt: The Risk Structure of Interest Rates*, 29 J. FIN. 449 (1974); Fischer Black & Myron Scholes, *The Pricing of Options and Corporate Liabilities*, 81 J. POL. ECON. 637 (1973); Edward I. Altman, *Financial Ratios, Discriminant Analysis and the Prediction of Corporate Bankruptcy*, 23 J. FIN. 589 (1968).

196. *See generally* Duffee, *supra* note 195 (modeling the pricing of default risk); Merton, *supra* note 195 (theorizing on the risk structure of interest rates).

slightly more than 60% of the assets collected by trustees are distributed to creditors.¹⁹⁷ The rest of the assets are eaten up by administrative costs, including about 9% paid directly to trustees and their firms, including for accounting fees and expenses.¹⁹⁸

In consumer bankruptcy, however, the largest effect on interest rates – and by extension, the largest benefit to creditors – seems to come from delaying or even deterring consumer bankruptcy altogether.¹⁹⁹ It is not, in other words, created by trustees, because trustees rarely discover assets for distribution in consumer bankruptcy. Even when they do, the cost of discovering assets tends to be high, and the actual return to creditors is correspondingly low. In the Jiménez study, out of the small fraction of consumer cases where trustees collected assets, 43% of those collected amounts were paid to the trustee and allied professionals.²⁰⁰ The remaining 57% was evidently insufficient to arouse creditor interest.²⁰¹ Indeed, barely half of the unsecured creditors even bothered to send in proofs of claims.²⁰²

To empirically quantify the high cost of locating assets in consumer bankruptcy, this Note uses national data from the USTP to create Figure 4, which shows the proportion of the overall asset collection that was paid for administrative expenses including trustee fees – that is, the percentage of asset collection that did not benefit any creditor – by decile of cases ranked by total assets.²⁰³ The

197. To calculate these percentages, we first summed up all distributions to priority, secured, and unsecured creditors for the cases that closed between 2015 and 2019 to get the total distribution to creditors. Then, we summed up gross receipts of these cases. Finally, we divided the total distribution to creditors by the total gross receipt. The result is a 62% distribution rate. USTP Data, *supra* note 113 (providing data from 2015-2019). Unfortunately, this dataset does not distinguish consumer cases from business cases, so we were unable to estimate the percentage for each subset.

198. To get the total distribution to trustees, we first summed up all distributions paid to Chapter 7 trustees, the trustees' firms, the trustees' accountants, and the UST as fees or reimbursements for expenses for cases closed between 2015 and 2019. Then, we summed up gross receipts of these cases. Finally, we divided the total distribution to trustees by the total gross receipt. The result is 9.27%. USTP Data, *supra* note 113 (providing data from 2015-2019).

199. See, e.g., Gross et al., *supra* note 156, at 1-5 (studying the effect of BAPCPA, which disincentivizes consumer filing); Igor Livshits, James MacGee & Michèle Tertilt, *Consumer Bankruptcy: A Fresh Start*, 97 AM. ECON. REV. 402, 406-07 (2007) (modeling the trade-off between lower interest rates and the availability of bankruptcy).

200. Jiménez, *supra* note 68, at 803.

201. Under the absolute priority rule, even this 57% must first be distributed to bankruptcy counsel, child support, and alimony, etc., before a typical unsecured creditor (e.g., a credit card company or a student-loan lender) can receive anything. See 11 U.S.C. § 507 (2018).

202. Jiménez, *supra* note 68, at 807.

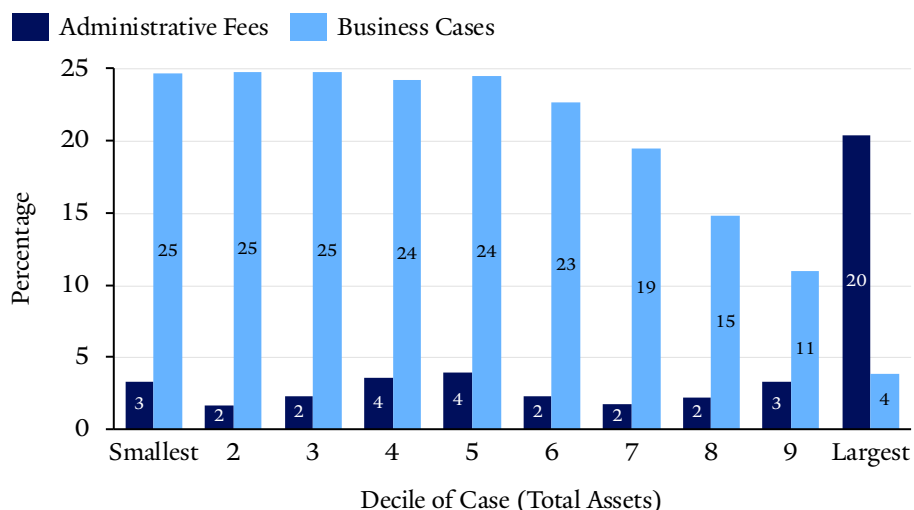
203. For the calculation, see *supra* note 197. For total assets used to split deciles, see USTP Data, *supra* note 113.

x-axis shows the decile of cases, that is, the “smallest” bar shows the bottom 10% of cases by total assets, and the “largest” bar shows the top 10% of cases by total assets. Because the USTP does not distinguish business and consumer cases in the data it publishes, it is practically impossible to hone in on consumer cases – yet another example of how Chapter 7’s failure to distinguish causes inefficiencies in the oversight of trustees’ work. However, as a general trend, the largest cases (i.e., the cases with the highest gross receipts and total assets) are disproportionately business cases,²⁰⁴ and, there, trustee fees account for a much smaller proportion of total distributions.²⁰⁵ Therefore, even though we cannot distinguish business cases from consumer cases in this dataset, the difference between large and small cases can shed light on the difference between business and consumer cases. This corroborates this Note’s hypothesis that the marginal effect on interest rates of trustees’ investigative work in consumer cases is not as pronounced as in business cases.²⁰⁶

204. The dark blue bars of Figure 4 were calculated from the FJC Data, *supra* note 6. We first split all Chapter 7 asset cases closed between 2017 and 2019 into ten deciles by the total value of assets. Then, we calculated the percentage of each decile of cases that were business cases. Finally, we plotted these percentages in Figure 4.

205. *See infra* Figure 4.

206. One might also posit a process whereby a business trustee’s investigations are influenced by the involvement of other bankruptcy professionals. On that view, it is the involvement of the professionals, rather than the marginal dollar spent on trustee investigation, that is the primary cause of business distributions. However, no matter what the other bankruptcy professionals do, it is eventually the trustee’s responsibility to administer their claims. Therefore, the help from other bankruptcy professionals makes business trustees’ work even more efficient, as the trustees can do more work within the same amount of time.

FIGURE 4. ADMINISTRATIVE FEES AS A PERCENTAGE OF TOTAL DISTRIBUTION MADE BY TRUSTEES

Instead, the socioeconomic benefit that trustees create in consumer bankruptcy is in “achiev[ing] the ideal of individualized justice when the amount at stake in any particular dispute is small.”²⁰⁷ As consumer debtors have fewer assets compared to businesses, it can become too costly for individual creditors to coordinate.²⁰⁸ Moreover, when individual creditors do engage in collection, the imbalance of social power between creditors and debtors means that *collection* can easily become *coercion*.²⁰⁹ A debt collector might, for example, collect on a vulnerable consumer’s debt by placing harassing phone calls.²¹⁰ Therefore, soci-

207. Whitford, *supra* note 24, at 397.

208. Cf. ADLER ET AL., *supra* note 186, at 23 (“At its core, bankruptcy forces creditors to work together collectively[] [where] . . . [t]he creditors suffer from a collective action problem.”).

209. See *Fair Debt Collection Practices Act: BCFP Annual Report 2019*, BUREAU CONSUMER FIN. PROT. 8, 16 & tbl.1 (Mar. 2019), https://files.consumerfinance.gov/f/documents/cfpb_fdcpa_annual-report-congress_03-2019.pdf [<https://perma.cc/JTG3-AQSK>]. The Bureau of Consumer Financial Protection’s report on consumer complaints is confirmed by anecdotal evidence, which also shows that collectors sometimes deploy extralegal collection practices whereby they threaten to exploit the debtor’s lack of legal knowledge, see, e.g., JAKE HALPERN, *BAD PAPER: CHASING DEBT FROM WALL STREET TO THE UNDERWORLD* 163 (2014) (describing “the Buffalo Talk-Off,” an “illegal, . . . but common, strategy” whereby the debtor is told that an arrest or involuntary court appearance is imminent if they do not repay), or pursue unenforceable debt or even debt not owed, *id.* at 114, 158, 164, 234.

210. Cf. HALPERN, *supra* note 209, at 50-52 (detailing how a single mother was harassed by an illegitimate creditor who was enforcing “stolen paper”).

ety benefits from deferring the distribution and administration of a debtor's estate to an intermediary, the trustees. As most consumer cases are simple and routine, the trustees' work, if properly incentivized, can add tremendous value by saving judges' time for more complicated questions.

As this Note discusses below in Section IV.A, to maximize the socioeconomic value of trustee work, Chapter 7 should distinguish between business and consumer bankruptcies. Encouraging or aiding trustees to aggressively pursue assets makes more sense in business bankruptcy, while monitoring and streamlining collection procedures makes more sense for consumer cases.

C. Trustees Do Drastically Different Work in Consumer and Business Bankruptcies

Formally, the Bankruptcy Code assigns the same list of "jobs" to Chapter 7 trustees, whether they work on consumer or business cases.²¹¹ However, in practice, trustees' day-to-day work varies significantly based on the type of case. As around 94% of consumer cases involve no unencumbered assets to distribute,²¹² a trustee's work after reviewing the debtor's financial status is typically limited to ensuring that the paperwork is correctly filed with the court.²¹³ Despite the large number of cases, consumers tend to have similar assets—houses, cars, tax refunds, etc.²¹⁴ For this reason, trustees can often conduct their investigations by reviewing standardized schedules,²¹⁵ tax documents, and other forms.²¹⁶

211. See 11 U.S.C. § 704 (2018).

212. See *supra* notes 7-8 and accompanying text.

213. See Exec. Off. for U.S. Trs., *supra* note 62, § 4(C)(2).

214. We obtained these examples by looking at random Chapter 7 debtors' records on Public Access to Court Electronic Records (PACER), particularly their Schedule A/B, which is a schedule that includes lists of the debtor's major assets. PACER Data, *supra* note 131, at Sched. A/B. A standardized Schedule A/B is provided by the U.S. Courts. *Official Form 106A/B*, U.S. CTS. (Dec. 1, 2015), https://www.uscourts.gov/sites/default/files/form_b106ab.pdf [<https://perma.cc/YD4Z-BBBN>].

215. When a debtor files for bankruptcy, she is required to attach to her petition several schedules that summarize her financial situation. For example, Schedule A/B lists the debtor's properties, such as vehicles and real estate. Schedule C asks the debtor to identify "exempt properties," which refers to assets that she is allowed to keep after bankruptcy under federal and state laws. In the rest of the schedules, the debtor is required to disclose her income and expenses as well as the debts she owes. These forms are then sent to the trustee for review. See 11 U.S.C. § 521(a) (2018) (stating that the debtor must "file" such documents).

216. Typical documents reviewed by a trustee include items such as pay stubs, bank statements, retirement account statements, loan documents, and proofs of property ownership. Baran Bulkat, *Documents to Bring to the Bankruptcy Meeting of Creditors*, ALLLAW (2021), <https://www.alllaw.com/articles/nolo/bankruptcy/documents-bring-meeting-of-creditors.html> [<https://www.alllaw.com/articles/nolo/bankruptcy/documents-bring-meeting-of-creditors.html>].

In contrast, about 33% of business cases are asset cases,²¹⁷ which means that the trustee must collect assets from the company, liquidate them, and distribute them based on the absolute priority rule.²¹⁸ Some cases are converted from Chapter 11,²¹⁹ creating legal and technical challenges not present in consumer cases. The trustee's work is less repetitive than in consumer cases because business assets vary from case to case. Efficiency demands that trustees have a high level of discretionary authority. While cutting costs and streamlining in consumer cases might be sensible, doing so in business cases risks undermining trustee discretion and slowing down the process.

Separating the regulation of trustees' work in consumer and business bankruptcies can promote efficiency and fairness without undermining the system, and requiring trustees to specialize in either consumer cases or business cases, or incentivizing them to do so, could facilitate expertise building and streamline trustees' practices in consumer cases. Arguably, a trustee specialized in consumer bankruptcy would benefit from minimizing overhead costs and hiring assistants who can process standardized documents. Consider the collection of tax refunds in consumer bankruptcy. It has long been established that a tax refund received after the filing date is considered an asset of the estate,²²⁰ and empirical evidence suggests that tax refunds comprise a significant proportion of the assets recovered by trustees.²²¹ As discussed above, recent empirical evidence from NDIL suggests that tax refunds are effectively ignored by trustees in over 90% of consumer cases.²²²

[//perma.cc/RG8T-CHG9](https://perma.cc/RG8T-CHG9)]; see also U.S. BANKR. CT. E.D. MICH. LOC. R. 2003-2 (listing documents debtors are required to bring to the meeting of creditors).

217. For calculation of this percentage, see *supra* note 6.
218. See Douglas G. Baird, *Priority Matters: Absolute Priority, Relative Priority, and the Costs of Bankruptcy*, 165 U. PA. L. REV. 785, 786 (2017) (“The absolute priority rule is the organizing principle of the modern law of corporate reorganizations. If one creditor has priority over another, this creditor needs to be paid in full before the other is entitled to receive anything. It does not matter whether payment takes the form of cash from a sale or new securities in a reorganization. Priority is absolute. By its nature, priority requires a rank-ordering of claims. Such is the conventional thinking about priorities in bankruptcy.” (footnotes omitted)).
219. Between 2010 and September 2020, 17% of business asset cases closed under Chapter 7 were converted from Chapter 11. To obtain this number, we first counted the number of business Chapter 7 asset cases that were originally filed under Chapter 11, and then divided it by the total number of business Chapter 7 asset cases filed between 2010 and September 2020. FJC Data, *supra* note 6.
220. *Kokoszka v. Belford*, 417 U.S. 642, 642, 652 (1974) (establishing that a tax refund is property of the estate).
221. Jiménez, *supra* note 68, at 808 (finding that tax refunds collected by trustees amounted to more than the proceeds from “the sale of cars, stocks, insurance policies, personal or business property, and interests in lawsuits” combined).
222. *Supra* note 139 and accompanying text.

This issue cannot be effectively addressed through a uniform increase in trustee payment because doing so would not decrease the cost of collecting tax refunds. The trustees either do not know that they should collect the refund or actively choose not to because the cost of doing so outweighs the refund's value. As such, the most effective solution would be to formulate rules tailored to the specific issues of consumer bankruptcy and assign consumer cases to trustees with lower overhead costs. This would correct the misaligned incentives of the current system and solve issues like the variation in tax-refund collection.

D. Trustees Receive Less Judicial Oversight in Consumer Cases

Trustees interact differently with other parts of the judicial system depending on whether the debtor is a consumer or a business. This occurs because, intuitively, business creditors and debtors are better equipped to bring their claims to court, so trustees in business bankruptcy are more closely supervised by judges. A comprehensive study in 1991 estimated that, on average, judges spend about six minutes in total on a Chapter 7 consumer case and twenty-three minutes on a Chapter 13 case, compared to about twenty-four minutes on a business Chapter 7 case and seven-and-a-half hours on a business reorganization case under Chapter 11.²²³ There is no reason to believe that this imbalance of

223. Gordon Bermant, Patricia A. Lombard & Elizabeth C. Wiggins, *A Day in the Life: The Federal Judicial Center's 1988-1989 Bankruptcy Court Time Study*, 65 AM. BANKR. L.J. 491, 504 tbl.3 (1991). These numbers exclude time spent on adversarial proceedings – those disputes “instituted by a complaint rather than a bankruptcy petition” and which “receive[] [their own] unique docket numbers[s] when . . . filed with the clerk’s office” – but include time spent on “contested matters” that are not administratively separated from a given bankruptcy proceeding. *Id.* at 496. Setting adversarial proceedings aside, the authors clarify:

In this study, case-related time refers to time judges spent on specifiable filings (that is, filings that can be identified by docket number) in one or more of four categories of judicial activity. The four categories were designed to contain activities that would ordinarily or intuitively be described as directly related to a case: relief from stay activities, reviewing and signing orders, plan confirmation activities, and other case and adversary proceeding activities. These do not include time spent on other matters essential to running a court (e.g., court meetings and committee meetings), to maintaining judicial chambers with several employees (e.g., hiring and training new law clerks or conferring with a courtroom deputy or court reporter on general matters) or to sustaining collegial relationships with other members of the court.

Id. at 500. On average, judges spent about an hour and twenty-one minutes on adversarial proceedings related to discharge, and two hours and ten minutes on all other adversarial proceedings. *Id.* at 504 tbl.3. Of course, the study is not without its critics. See, e.g., George M. Huyler & Francis G. Conrad, *A Critique of the Bankruptcy Court Time Study*, 67 AM. BANKR. L.J. 49, 52-55 (1993) (critiquing the study’s reliance on judges’ self-reported timesheets and the asset thresholds that the authors used to classify Chapter 11 cases).

attention has improved over the years.²²⁴ This topic has become particularly relevant in recent years, as judges and scholars debate the possibility of achieving “procedural justice” in a consumer-bankruptcy system from which judges are largely absent.²²⁵

The primary reason that consumer bankruptcy receives so little attention from judges is that consumers and their creditors rarely bring their claims to court.²²⁶ This gives trustees in consumer cases broad power to dispense with consumer cases as they see fit.²²⁷ In contrast, in business bankruptcy, the debtors and creditors are usually equipped with sophisticated teams of bankruptcy lawyers, accountants, and professional managers.²²⁸ Their adversarial or quasi-adversarial relationship with the trustee ensures that trustee actions are brought before judges more often. In NDIL, for example, an average business case requires 3.2 times more motions from the trustee than the average consumer case.²²⁹ In hearing these motions, judges can more directly supervise trustee actions in a manner not possible for consumer cases.

Judges might also overlook consumer cases because business cases are more enticing. Business bankruptcies tend to be more sensational and complicated,

224. Consider that judicial resources have only been stretched thinner over the years. See Benjamin Iverson, Jared A. Ellias & Mark Roe, *Estimating the Need for Additional Bankruptcy Judges in Light of the COVID-19 Pandemic*, 11 HARV. BUS. L. REV. ONLINE 1, 1 (2020), https://www.hblr.org/wp-content/uploads/sites/18/2021/01/HBLR-Estimating-the-Need-for-Additional-Bankruptcy-Judges-Proof_2.pdf [<https://perma.cc/DH8W-FFVM>] (arguing that the bankruptcy system may need at least fifty additional temporary judges just to maintain the average workload at 2010 levels).

225. See, e.g., Foohey, *supra* note 57, at 2316-18 (advocating for such procedural justice); Jonathan C. Gordon, *A (Not New) Response to A New Deal for Debtors*, 94 AM. BANKR. L.J. 507, 507-09 (2020) (responding to Foohey’s article).

226. Cf. Bermant et al., *supra* note 223, at 496 n.8, 520-21 (“Our use of asset categories [for purposes of measuring judicial time spent on bankruptcy cases] was based on the idea that there will be more lawyer involvement in cases with larger assets and that judicial time-burdens are created directly by lawyer involvement.”).

227. *Supra* notes 58-63 and accompanying text.

228. See, e.g., Victoria M. Zunitch & Michael Hayes, *The Business of Bankruptcy*, J. ACCT. (Feb. 1, 2002), <https://www.journalofaccountancy.com/issues/2002/feb/thebusinessofbankruptcy.html> [<https://perma.cc/U64X-JJMH>] (discussing the “exclusive club” of professionals that support business debtors filing for bankruptcy).

229. On average, a consumer case requires 0.73 motions from the trustee; a business case requires 2.3 motions from the trustee. To obtain these numbers, we downloaded from PACER the docket entries for Chapter 7 cases filed between 2008 and 2017 in NDIL and identified those filed by the trustee. See PACER Data, *supra* note 131.

with large dollar amounts or national brands.²³⁰ Although less than 1% of Chapter 7 cases from the past decade were filed by corporations holding business debt,²³¹ consumer bankruptcies are relatively understudied. Widely circulated bankruptcy casebooks focus primarily on business cases.²³²

Accordingly, forces that would ordinarily promote fairness, such as judicial oversight and adversarial proceedings, are weak or absent altogether in consumer bankruptcy. For creditors, judicial absence means that assets that could have been collected, such as accrued tax refunds, are routinely ignored.²³³ For debtors, judicial absence means that trustees can engage in aggressive collection, treating similarly situated cases in different ways.²³⁴ For these reasons, trustees' discretionary decisions in consumer bankruptcy should be more closely regulated than in business bankruptcy.

230. See, e.g., Richard A. Oppel Jr. & Andrew Ross Sorkin, *Enron's Collapse: The Overview*; *Enron Corp. Files Largest U.S. Claim for Bankruptcy*, N.Y. TIMES (Dec. 3, 2001), <https://www.nytimes.com/2001/12/03/business/enron-s-collapse-the-overview-enron-corp-files-largest-us-claim-for-bankruptcy.html> [<https://perma.cc/BM9Y-4SUM>] (describing the \$50 billion Enron bankruptcy). Enron would later become a household byword for corruption and mismanagement. See Troy Segal, *Enron Scandal: The Fall of a Wall Street Darling*, INVESTOPEDIA (May 31, 2021), <https://www.investopedia.com/updates/enron-scandal-summary> [<https://perma.cc/PUJ6-5EFD>].

231. From 2008 to 2019, only 3.3% of all Chapter 7 cases were filed with primarily nonconsumer debt, which includes 2.4% filed by individuals holding business debt. Therefore, less than 1% of all Chapter 7 cases were filed by corporations holding business debt. We obtained these percentages by first counting the number of Chapter 7 cases filed between 2008 and 2019 where the debtor's debt was primarily nonconsumer debt, and then counting the number of Chapter 7 cases filed between 2008 and 2019 where the debt was primarily nonconsumer but the legal form of the debtor was an individual. Finally, we divided these two numbers by the total number of Chapter 7 cases filed between 2008 and 2019. See FJC Data, *supra* note 6.

232. See generally ADLER ET AL., *supra* note 186 (containing illustrative cases on bankruptcy law); DANIEL J. BUSSEL, DAVID A. SKEEL, JR. & MICHELLE M. HARNER, *BANKRUPTCY* (11th ed. 2020) (same); MARGARET HOWARD & LOIS R. LUPICA, *BANKRUPTCY: CASES AND MATERIALS* (6th ed. 2015) (same).

233. In NDIL, for example, it is estimated that over 90% of collectible tax refunds were ignored. *Supra* note 139 and accompanying text.

234. Cf. Morrison et al., *supra* note 10, at 23-24 & tbl.3 (showing the significant difference between trustees disfavored by trustee-shopping). Even with existing levels of judicial oversight, trustees' asset collection rates can differ by one *order of magnitude* within the same office in the same district, and some trustees can take 40% more time than others to finish a case. We estimated this from Figure 7 of Morrison et al. *Id.* at 33 fig.7.

IV. PROPOSED SOLUTIONS

Based on the empirical evidence and normative arguments discussed above, this Note proposes two policy changes. First, the Chapter 7 trustee-compensation scheme should not be the same for consumer and business bankruptcies. Second, Chapter 7 trustees should be allowed, and even required, to specialize in either consumer or business bankruptcy. Splitting Chapter 7 trustees into consumer specialists and business specialists will not only lower the cost of case administration, but also make it possible to implement effectively distinctive regulations for each type of case. These changes would increase procedural justice and systemic efficiency by making trustees more neutral and Chapter 7 outcomes less heterogeneous.

A. Policy Recommendations

1. Flat Fees for Consumer Cases, Variable Fees for Business Cases

As Section II.A detailed, the current one-size-fits-all compensation scheme includes both a flat fee and a variable component.²³⁵ The flat fee comes primarily from debtors' filing fees, while the variable component is a proportion of the unencumbered assets that the trustee administers.²³⁶ The result is that Chapter 7 trustees are undercompensated for consumer cases,²³⁷ and they focus their attention on getting lucrative business cases. The 2020 reforms correctly raised flat fees.²³⁸ However, doing so did not resolve the problem that investigating debtors' financials is more lucrative in business bankruptcy than consumer bankruptcy. In other words, trustees remain incentivized to brush aside consumer cases to spend more time on business cases.

This Note proposes an alternative: differentiate the compensation scheme for consumer and business bankruptcy. Tailoring the fee structure to the trustees' work in consumer and business bankruptcy ensures that trustees are compensated for the work that brings the most socioeconomic value: the adjudication of small-stakes claims in consumer bankruptcy and the collection and distribution of assets in business bankruptcy. Moreover, it solves the problem that, because

²³⁵ See *supra* Section II.A.

²³⁶ See 11 U.S.C. § 326(a) (2018); 11 U.S.C.A. § 330 (West 2021); *supra* Part II.

²³⁷ Cf. Flynn, *supra* note 122, at 92 (“[I]t is clear that their compensation has not kept up with the amount of work that is expected of them.”).

²³⁸ Bankruptcy Administration Improvement Act of 2020, Pub. L. No. 116-325, § 3, 134 Stat. 5086, 5087-89 (2021).

trustees are disproportionately compensated by business bankruptcy, the administration of consumer bankruptcy is often undervalued or outright ignored.

For consumer bankruptcy, the flat fee should be set higher so as to reflect the minimum amount of time a trustee spends on nonasset cases, and the fee level should be reset every other year to match the market rate (i.e., the comparable hourly rate for private lawyers).²³⁹ The variable component, if retained, should have narrower brackets to reflect the fact that most consumers have less than \$5,000 of distributable assets,²⁴⁰ which is the lowest asset bracket under the current system. The percentage rate of the lowest bracket, however, should be substantially higher to cover trustees' sunk cost for investigation.²⁴¹

For business bankruptcy, on the other hand, the flat fee serves no purpose. The fact that trustees are willing to work essentially for free for the chance to be included in the trustee panel and so become eligible for lucrative business cases indicates that the current scheme is awarding more fees to trustees in business bankruptcy than necessary.²⁴² Arguably, if trustees were properly compensated for consumer bankruptcy after the proposed adjustment, it might make economic sense to lower the fees charged in business bankruptcy.²⁴³

Admittedly, the nature of consumer bankruptcy creates the possibility that the fees collected may not on their own be sufficient to fully compensate the trustees for their work. As previously mentioned, the current scheme imple-

239. Alternatively, the fee may be adjusted according to inflation indices like the Consumer Price Index. *Consumer Price Index*, BUREAU LAB. STAT., <https://www.bls.gov/cpi> [<https://perma.cc/NQ8P-NLBQ>].

240. In fact, over 50% of all asset cases closed in 2018 had distributable assets less than or equal to \$5,000. To get this number, we divided the number of asset cases closed in 2018 where less than \$5,000 was distributed by the total number of asset cases closed in 2018 reported in the USTP Data. USTP Data, *supra* note 113. As shown in Figure 4, most of these small cases were consumer cases. See *supra* Figure 4.

241. Cf. Flynn, *supra* note 122, at 92 (explaining that fees and salaries related to bankruptcy cases have increased in the past twenty years).

242. Cf. Antill, *supra* note 25, at 28 (“The Bankruptcy Administration Improvement Act of 2020 was signed into law on January 12, 2021. The act establishes a Chapter 7 Trustee Fund to pay trustees an additional \$60 in all cases. According to the Justice department, 20 applicants applied for each open Chapter 7 trustee position prior to the act, suggesting that the additional \$60 is not necessary to induce trustee participation. This increase in fixed compensation could thus be feasibly offset by a reduction in trustee commissions without making trustees quit. My results suggest that this reduction in commissions would greatly benefit creditors.” (footnotes omitted)).

243. Cf. *id.* at 2 (“[T]he legally mandated commission [set forth in 11 U.S.C. § 326(a) (2018) and 11 U.S.C.A. § 330(a)(7) (West 2021)] is substantially higher than the optimal commission, causing large creditor losses.”).

mented by the 2020 BAlA involves subsidizing consumer bankruptcy using proceeds from business bankruptcy.²⁴⁴ By narrowing the brackets of the variable component and increasing the fee ratio, this Note’s proposed rule better incentivizes trustees to seek hidden assets—such as the 90% of tax refunds that are currently ignored in Chicago bankruptcy—but subsidies from Chapter 11 cases as implemented by the Act may still be necessary or desirable.²⁴⁵ If that is the case, the subsidy could be done more efficiently by expanding the Chapter 7 Trustee Fund along the lines of the policy change in January 2021 regarding Chapter 11 cases.²⁴⁶ For example, businesses could be charged a contingent fee that goes to the Chapter 7 Trustee Fund just like the quarterly fee collected from Chapter 11,²⁴⁷ which would be distributed pro rata among all Chapter 7 trustees explicitly to keep the system afloat.²⁴⁸ This avoids the dilemma that, by “rewarding” trustees with business cases, trustees might become reluctant to carry out their duties in consumer bankruptcy.

This proposal directly addresses the counterargument that, in the absence of Chapter 7 intermingling, trustees would not otherwise concern themselves with consumer bankruptcy. It is, of course, true that some trustees might not continue to work on consumer cases if fees were not fully equalized. Yet that would be a desirable consequence of disentanglement; as explained in Section IV.A.ii, trustees who fail to specialize their business model to handle consumer cases simply should not be in the business of handling them. There may be some extent to which maintaining a consumer-bankruptcy system requires consumer cases to be subsidized by business cases; otherwise, there may be too few trustees interested in consumer work. However, insofar as a subsidy is necessary, it is better implemented through a system that directly collects money from the business cases for redistribution among consumer cases, without commingling the two.

2. Trustee Specialization

Bearing in mind the differential trustee incentive structure, an even more radical change would be to split the panel of trustees assigned to consumer and business cases into two separate specialized panels. Because trustees’ work varies

²⁴⁴ See *supra* text accompanying notes 102-111; see also 28 U.S.C.A. § 589a(f) (West 2021) (setting forth the subsidy system).

²⁴⁵ After all, “[r]educing [business] trustee commissions from the current level might induce trustees to quit.” Antill, *supra* note 25, at 2.

²⁴⁶ See *supra* text accompanying note 104.

²⁴⁷ See 28 U.S.C.A. §§ 589a(f)(1)(C), 1930(a)(6) (West 2021).

²⁴⁸ Cf. 11 U.S.C.A. § 330(e) (West 2021) (distributing the quarterly Chapter 11 fees pro rata among Chapter 7 trustees).

between consumer and business bankruptcy, requiring the same trustees to handle both makes it difficult to build expertise and improve a trustee's business model.

For example, an ideal trustee for consumer bankruptcy is one with low overhead costs.²⁴⁹ As most consumer cases require little more than routine work, the trustee can delegate a substantial proportion of the responsibilities to assistants and paralegals.²⁵⁰ For some regions, having a suburban office may be the key to profiting in consumer cases because it is cheaper and closer to residential areas in the region.²⁵¹ In addition to supporting the trustee's work, the firm can specialize in related legal services such as personal bankruptcy, foreclosure, and consumer debt.²⁵² Income generated by these auxiliary services can supplement the trustees' compensation from the bankruptcy system.²⁵³

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249. Courts have been reluctant to reimburse these expenses. See, e.g., *In re Rauch*, 110 B.R. 467, 476 (Bankr. E.D. Cal. 1990) (“[A]lthough the [Chapter 7] [t]rustee is entitled to engage paraprofessionals to assist him and have paraprofessionals paid out of the estate, secretarial, stenographic, clerical and routine messenger services are overhead expenses which are not compensable or reimbursable.” (citing 11 U.S.C. § 330(a)(1), (2) (1990))); *Sousa v. Miguel (In re U.S. Tr.)*, 32 F.3d 1370, 1374 (9th Cir. 1994) (“Activities such as reviewing mail, making deposits and disbursements and reconciling bank statements appear to be clerical in nature’ and are overhead expenses to be assumed and borne by the Trustee.” (quoting *In re Orthopaedic Tech., Inc.*, 97 B.R. 596 (Bankr. D. Colo. 1989))).
250. Administrative paperwork is a central part of consumer bankruptcy: “[W]hen struggling, bankrupt consumers hand over much-needed funds to their lawyers, they are paying for . . . the fact that much of the administrative work necessary to process their bankruptcies will be completed by people they have hired, rather than by government officials operating under the pressures of bureaucratic disinterest.” Angela Littwin, *The Affordability Paradox: How Consumer Bankruptcy’s Greatest Weakness May Account for Its Surprising Success*, 52 WM. & MARY L. REV. 1933, 1941 (2011).
251. Many Chapter 7 trustees are located in urban areas. See *Chapter 7 Panel Trustees Office Locator*, U.S. DEP’T JUST., https://www.justice.gov/ust/eo/private_trustee/locator/7.htm [<https://perma.cc/F3SB-QUK8>]. In contrast, more than half of consumer-bankruptcy attorneys are located in rural or suburban areas. Ronald L. Burdge, *United States Consumer Bankruptcy Law: Attorney Fee Survey States Report 2017-2018*, BURDGE L. OFF. CO. 26 (Jan. 19, 2020), <https://www.nclc.org/images/pdf/litigation/tools/report-atty-fee-survey.pdf> [<https://perma.cc/DY92-2RHZ>]. Trustees who want to receive business cases are pressured to stay in expensive urban areas. Cf. Lupica, *supra* note 25, at 110 (“Cases with assets to distribute mostly occur in urban areas.” (quotation omitted)).
252. In fact, consumer-bankruptcy attorneys are already taking advantage of this synergy. Burdge, *supra* note 251, at 21 (reporting that areas of consumer law regularly handled by consumer-bankruptcy attorneys are credit rights (58%), mortgage (56%), vehicles (34%), and the Telephone Consumer Protection Act (24%)). There is no reason why consumer trustees should not do the same.
253. “[A]n attorney handling consumer bankruptcy cases, where some fees may be externally monitored, often handles associated financial and other problems of clients and may have the opportunity to do so at higher hourly rates than they charge for their bankruptcy work.” *Id.*

None of the above makes sense for a trustee specialized in business bankruptcy. Ideally, her office would have access to skilled accountants and other professionals to assist her investigation into a business's financial affairs and her evaluation of its assets.²⁵⁴ Her office may be located in the commercial center of the city, and she herself would likely be a business lawyer.²⁵⁵ Instead of honing in on administrative cost-cutting, her focus would likely be on how to efficiently collect, liquidate, and distribute business assets.²⁵⁶ If we compare these two models, we see that consumer and business cases require different—and often incompatible—skill sets and resources. An office capable of administering sophisticated business cases does not necessarily have the setup to cater to consumer debtors' needs or provide profitable services.

Another upside of specialization would be better-customized regulations for business and consumer liquidations. Because consumer trustees are likely to earn only a flat fee that does not vary with the quality of their work,²⁵⁷ the UST should supervise them more closely. For example, the UST might monitor consumer trustees' asset case rates, case lengths, and the frequency with which they collect tax refunds.²⁵⁸ In contrast, business trustees are compensated according to the thoroughness of their work and are subject to heightened judicial and professional monitoring, and so should enjoy a higher level of discretion to facilitate the administration of complex business cases.

Facilitating specialization would benefit the trustees themselves, but it would also make it possible for Chapter 7 to properly account for the different needs of consumers and businesses. Trustees, just like other lawyers, have the most immediate impact on human debtors. Chapter 7 has been rightly criticized for in-

254. In 2018, the top 20% of cases by size (including most business cases) involved expenditures of \$18,272 per case to hire professionals, in contrast to merely \$92 per case for the smaller cases. USTP Data, *supra* note 113. These numbers were calculated by taking the average of professional fees from the corresponding group as reported in the USTP Data. The size of the case is measured by the case's gross receipts. For more information on professionals that trustees should hire, see John Silas Hopkins, III, *Effective Review of Compensation in Large Bankruptcy Cases*, 88 AM. BANKR. L.J. 127, 155-61 (2014).

255. Cf. Exec. Off. for U.S. Trs., *supra* note 62, § 4(C) (“The trustee must be familiar with the definition of property of the estate as set forth in section 541. Under section 541, all legal and equitable interests of the debtor, wherever located and by whomever held, are property of the estate.”).

256. See Lubben, *supra* note 52, at 68 (“The theme in [business] chapter 7 is the speedy collection, reduction to cash, and distribution of the debtor's assets.”).

257. See *supra* Part II.

258. Cf. Morrison et al., *supra* note 10, at 33 fig.7 (providing figures that demonstrate serious variations between trustees along a variety of metrics).

sufficiently protecting “people’s rights to take care of themselves and their children while they are in the bankruptcy process.”²⁵⁹ This is hardly surprising. A system configured principally for business debtors will, as a matter of necessity, ignore consumer-specific needs. Should trustees be allowed to adjourn the 341 meetings if it would be time-consuming or expensive for the consumer to drive back to the trustee’s office another time?²⁶⁰ How much should trustees disclose about a debtor’s assets in court filings if disclosure will cause that debtor to suffer from social stigma?²⁶¹ What should the trustees do if the debtor is suicidal?²⁶² Should they liquidate a debtor’s house if doing so would render a debtor’s small children homeless?²⁶³

These are granular and diverse questions best answered by each individual trustee exercising her discretionary judgment. They are also doomed to be ignored if trustees must weigh answering them against ignoring them to work on a simultaneous business case. Specialization would allow the UST to select trustees that are best suited for consumer cases—that is, trustees who will have a business model that enables just, ethical, and efficient management of consumer cases.

Specialization is precluded by the current system because participation in consumer bankruptcy is mandatory and the fees generated by consumer cases

259. Elizabeth Warren, *Fixing Our Bankruptcy System to Give People a Second Chance*, WARREN DEMOCRATS, <https://elizabethwarren.com/plans/bankruptcy-reform> [<https://perma.cc/C8PS-TD7Q>]; see also Press Release, Sen. Elizabeth Warren, Warren and Nadler Introduce the Consumer Bankruptcy Reform Act of 2020 (Dec. 9, 2020), <https://www.warren.senate.gov/newsroom/press-releases/warren-and-nadler-introduce-the-consumer-bankruptcy-reform-act-of-2020> [<https://perma.cc/4GW8-BDQY>] (introducing the CBRA and emphasizing that the bill will “[e]nsure that filers can care for themselves and their families during the bankruptcy”).

260. See *supra* note 190 and accompanying text.

261. See Teresa A. Sullivan, Elizabeth Warren & Jay Lawrence Westbrook, *Less Stigma or More Financial Distress: An Empirical Analysis of the Extraordinary Increase in Bankruptcy Filings*, 59 STAN. L. REV. 213, 242-44 (2006) (pointing out that bankruptcy records are getting easier to access due to digitalization but “84.3% of families filing for bankruptcy indicated that they ‘would be “embarrassed” or “very embarrassed” if their families, friends, or neighbors learned of their bankruptcy” (quoting ELIZABETH WARREN & AMELIA WARREN TYAGI, *THE TWO-INCOME TRAP: WHY MIDDLE-CLASS MOTHERS AND FATHERS ARE GOING BROKE* 213 n.13 (2004))).

262. See, e.g., Ronald C. Sykstus, *Consumer Bankruptcy, and Chapter 13 and Chapter 7 Filings*, in BEST PRACTICES FOR FILING CHAPTER 13, at 69, 69 (2016) (describing a case with a suicidal debtor).

263. For an in-depth examination of the role that children play in bankruptcy, see Elizabeth Warren, *Bankrupt Children*, 86 MINN. L. REV. 1003 (2002).

alone are usually too low to sustain a trustee's firm.²⁶⁴ Therefore, the change proposed here would be most effective if it were combined with an increase in trustee compensation for consumer cases, such as the 2020 BAlA's increase in flat fees.²⁶⁵ While specific rules are still being promulgated and the final execution of the pay raise is still unclear, it may be enough to enable trustee specialization.

The fact that most trustees in the current system are not interested in specializing in consumer cases and are not equipped to do so suggests that it will likely be difficult to convert enough current trustees to specialize in consumer cases. Therefore, besides providing a reasonable fee structure, nonmonetary support must be provided to attract new trustees to specialize in consumer cases. Such support could be provided in many ways. For example, the USTs could promote best practices for consumer trustees and encourage current consumer-bankruptcy lawyers to become trustees, just as business lawyers are currently recruited to become business trustees.²⁶⁶ The USTs could expand and formalize existing training programs to cater to consumer trustees' practice. One example of such training programs is DOJ's National Bankruptcy Training Institute under the Executive Office for U.S. Trustees, which currently offers courses on a range of topics such as civil and criminal trial advocacy. By creating synergies between trustees' work and the work of lawyers in related fields, the USTs could make the job more attractive. The USTs could also promote the job through organizations formed by the trustees themselves, such as the National Association of Bankruptcy Trustees. The USTs could expand the use of these informal venues to promote profitable business models for current and prospective trustees to adopt.

B. *Advantages Over Other Policy Proposals*

As discussed above, consumer bankruptcy has been in the spotlight since the COVID-19 pandemic hit the United States.²⁶⁷ As the specter of a consumer-bankruptcy tidal wave grows,²⁶⁸ proconsumer theories have begun to shift the

²⁶⁴. See Flynn, *supra* note 122, at 92; Holtschlag, *supra* note 20, at 71; cf. Antill, *supra* note 25, at 3 (“[C]orporate creditors subsidize unrelated individual debtors through Chapter 7 trustee compensation practices.”).

²⁶⁵. See Bankruptcy Administration Improvement Act of 2020, Pub. L. No. 116-325, § 3(e)(B)(i), 134 Stat. 5086, 5087-89 (2021) (adding 28 U.S.C.A § 589a(f)(1)(C) (West 2021) and 11 U.S.C.A § 330(e) (West 2021)).

²⁶⁶. For example, it has been reported that many trustees work at big law firms that focus primarily on businesses. Morrison et al., *supra* note 10, at 5.

²⁶⁷. See *supra* notes 153-160 and accompanying text.

²⁶⁸. See *supra* note 175-176 and accompanying text.

tenor of proposed policy changes. For example, the Consumer Bankruptcy Reform Act of 2020 (CBRA),²⁶⁹ introduced in both the Senate and the House in December 2020 by congressional Democrats Elizabeth Warren and Jerrold Nadler, respectively, proposed to eliminate the bifurcated consumer-bankruptcy system altogether.²⁷⁰ In place of the current consumer-bankruptcy system, the CBRA proposed a new “Chapter 10” that is neither solely reorganization nor liquidation.²⁷¹ The new system would have made it easier for consumers to afford bankruptcy representation,²⁷² allowed debtors to get their home mortgages and car loans modified,²⁷³ and even routinized the discharge of student-loan debts.²⁷⁴ The CBRA has not yet been reintroduced to either chamber of the most recent Congress, but Senator Warren and Representative Nadler’s desire to “cancel” consumer bankruptcy and replace it with an entirely new system is shared by some academics.²⁷⁵ Nevertheless, positions like theirs are sometimes opposed by others as unfeasible.²⁷⁶ For this reason, a reintroduced CBRA is unlikely to make much political headway unless circumstances change substantially.

By contrast, one important advantage of this Note’s proposals is that they are overwhelmingly within the immediate power of the USTs to implement. Congress mostly delegates the regulation of trustees to the USTs,²⁷⁷ and they generally do not require congressional permission to change trustee guidelines.²⁷⁸ Significantly, the Bankruptcy Code does not preclude the USTP from

269. Consumer Bankruptcy Reform Act of 2020, S. 4991, 116th Cong. (2020); Consumer Bankruptcy Reform Act of 2020, H.R. 8902, 116th Cong. (2020).

270. S. 4991 §§ 101-108; H.R. 8902 §§ 101-108.

271. S. 4991 § 102; H.R. 8902 § 102.

272. S. 4991 § 101(b)(4); H.R. 8902 § 101(b)(4).

273. S. 4991 § 101(b)(6)-(7); H.R. 8902 § 101(b)(6)-(7).

274. S. 4991 § 101(b)(8); H.R. 8902 § 101(b)(8).

275. See, e.g., Letter from Seventy-Four Law Professors to Elizabeth Warren, U.S. Sen. for Mass. (Dec. 14, 2020), <https://www.creditslips.org/files/cbra-law-prof-letter-in-support.pdf> [<https://perma.cc/88NW-BNQ3>] (writing in support of the CBRA).

276. See Gordon, *supra* note 225, at 507 (critiquing Foohey’s proposal for an administrative agency, Foohey, *supra* note 57, at 2343, and “suggesting a lighter, more flexible proposal: a framework for consumer debtors to submit their stories to the court, much like large, corporate debtors generally do at the beginning of their bankruptcy cases”). For papers criticizing the system without prescribing systemic reforms, see, for example, Jean Braucher, Dov Cohen & Robert M. Lawless, *Race, Attorney Influence, and Bankruptcy Chapter Choice*, 9 J. EMPIRICAL LEGAL STUD. 393, 423-25 (2012); and Katherine M. Porter, *The Pretend Solution: An Empirical Study of Bankruptcy Outcomes*, 90 TEX. L. REV. 103, 111-16 (2011).

277. See *supra* note 81 and accompanying text.

278. 28 U.S.C. § 586(a) (2018) empowers the UST to “establish, maintain, and supervise” the private trustee panels and provides the criteria under which the UST is to fulfill those duties.

encouraging – or even outright imposing – trustee specialization. USTs are required to “appoint one disinterested person that is a member of the panel of private trustees established under section 586(a)(1) of title 28” as the interim trustee for a case,²⁷⁹ and they are also charged to “establish, maintain, and supervise a panel of private trustees that are eligible and available to serve as trustees in cases under chapter 7 of title 11.”²⁸⁰ They are not, however, obligated to assign consumer cases to all panel trustees. Accordingly, the trustee specialization proposed by this Note could be accomplished without the need for additional legislative action. Considering that few (if any) consumer-bankruptcy-friendly bills have made it through Congress since 1984, and the urgent need for a solution in light of the pandemic, the fact that this Note’s proposals do not *require* congressional input is a meaningful advantage.

The solution’s ease of implementation should not suggest that it is merely a stopgap fix that fails to address broader issues in the Chapter 7 system. Chapter 7’s entangled trustee system lies at the very heart of the statute. Consequently, splitting Chapter 7 trustees into consumer and business specialists is a crucial first step necessary for any kind of further reform. Importantly, this is true regardless of the direction Chapter 7 subsequently takes: whether Chapter 7 is to become more business friendly, more consumer friendly, or something else, it would be impossible to meaningfully alter Chapter 7 without first splitting up Chapter 7 trustees. Changes in any other direction would be stymied by the Chapter’s inefficient, inequitable commingling of consumer and business cases and the perverse incentive structure that it creates.

On the other hand, as previously mentioned, Congress appears to have implemented a typical stopgap solution in the 2020 BAIA. The 2020 Act “fixes” Chapter 7 by simply subsidizing – and thus perpetuating – its entangled system and incentive structure with money from Chapter 11’s largely unentangled system.²⁸¹ In doing so, it highlights the inadequacy of reforms that do not disentangle business and consumer trustees. The Act gave trustees a raise,²⁸² but failed to solve the fundamental problem that Chapter 7 incentivizes trustees to swiftly get to their next lucrative business case at the expense of the consumer cases along the way. In contrast, this Note’s proposal to split up Chapter 7 trustees into specialists would effectively dismantle the incentive structure that encourages

The statute conspicuously does not provide for any congressional oversight over the UST’s discretion to fulfill its duties.

279. 11 U.S.C. § 701(a)(1) (2018).

280. 28 U.S.C. § 586(a)(1) (2018).

281. Bankruptcy Administration Improvement Act of 2020, Pub. L. No. 116-325, 134 Stat. 5086 (2021).

282. See *supra* notes 104-105 and accompanying text.

destructive collection behaviors. In turn, the system would become more fair, efficient, and protective of vulnerable consumers.

Indeed, splitting up Chapter 7's trustees and regulating them separately might fix a variety of other broad problems identified by academics and politicians. For example, Chapter 7 consumer bankruptcy has been criticized as "procedurally bankrupt" – that is, lacking in dignitary legitimacy – because trustees are subjected to limited judicial oversight or adversarial proceedings.²⁸³ Relatedly, Chapter 7 has been criticized for the arbitrariness and wide divergence of its outcomes: for example, consumer-bankruptcy luminary Jean Braucher noted two decades ago that "[s]imilarly situated debtors, in terms of debt and income, end up with very different deals in bankruptcy,"²⁸⁴ and recent empirical scholarship has borne out her observation.²⁸⁵ As discussed in Section II.B, the current system fails to incentivize trustees to treat similarly situated debtors similarly.²⁸⁶ Trustees may instead do what is most convenient for them: within the same office, one trustee's asset collection rate might differ by a full order of magnitude from another's, while other trustees might take as much as 40% more time to finish a consumer case than their peers.²⁸⁷ Some reform proposals try to increase bankruptcy's dignitary legitimacy by calling for judges or even juries to participate more actively in consumer cases.²⁸⁸ But this is an inefficient solution because consumer bankruptcies tend to be heavily administrative. While they may be

283. See *supra* note 57 and accompanying text; see also *supra* Section III.D (discussing the lack of judicial oversight in Chapter 7); Nathalie Martin, *Bringing Relevance Back to Consumer Bankruptcy*, 36 EMORY BANKR. DEVS. J. 581, 620-22 (2020) (advocating for a "reconstructed vision of a discharge hearing [that] could make the system more humane"); Pamela Foohey, *Consumer Bankruptcy Should Be Increasingly Irrelevant – Why Isn't It?*, 36 EMORY BANKR. DEVS. J. 653, 662-64 (2020) (summarizing her reform proposals as a response to Professor Martin).

284. Jean Braucher, *Increasing Uniformity in Consumer Bankruptcy: Means Testing as a Distraction and the National Bankruptcy Review Commission's Proposals as a Starting Point*, 6 AM. BANKR. INST. L. REV. 1, 17 (1998).

285. Morrison et al., *supra* note 10, at 33 fig.7.

286. See *supra* Section II.B.

287. See *supra* note 234 and accompanying text.

288. Martin, *supra* note 283, at 620-22; Foohey, *supra* note 57, at 2317.

made procedurally fairer by judicial *involvement* (which would probably curb undesirable trustee behavior), they benefit little from judicial expertise.²⁸⁹ Moreover, court time is a limited, valuable resource,²⁹⁰ and it might be better spent in other ways.²⁹¹

This Note's proposals aim to secure dignitary legitimacy and uniform outcomes by making trustees more neutral—*similar* to judges, but without the attendant costs.²⁹² The first proposal calls for flat-fee-based compensation combined with regulation; the second proposal calls for professional specialization. In conjunction, these two proposals would eliminate the incentives trustees currently have to either rush debtors haphazardly through the process or wring out every penny from them. This Note's proposals might therefore increase procedural justice and harmonize outcomes for Chapter 7 debtors without raising process costs. Trustees would be well incentivized to not only treat like debtors alike, but to treat them all with dignity.

CONCLUSION

Consumer and business bankruptcy cases differ in many fundamental ways, but, under Chapter 7, both are administered by the same panel of trustees under roughly the same rules. For example, the compensation scheme is the same for both consumer and business cases, undervaluing trustees' work in consumer bankruptcy and overvaluing trustees' work in business bankruptcy. This Note questions the Chapter 7 status quo, casting doubt on the rationale—if any—behind having the same trustees administer both consumer and business cases under the same set of regulations. The fundamental differences between natural persons and businesses, the different socioeconomic benefits created and work

289. See *supra* Sections III.C, III.D; Gordon, *supra* note 225, at 510 (arguing that the lack of contested matters in consumer bankruptcy justifies less judicial oversight); *Chapter 7—Bankruptcy Basics*, U.S. CTS., <https://www.uscourts.gov/services-forms/bankruptcy/bankruptcy-basics/chapter-7-bankruptcy-basics> [<https://perma.cc/TU34-FR5U>].

290. See Marin K. Levy, *Judicial Attention as a Scarce Resource: A Preliminary Defense of How Judges Allocate Time Across Cases in the Federal Courts of Appeals*, 81 GEO. WASH. L. REV. 401, 407 (2013); see also *Judicial Economy*, BLACK'S LAW DICTIONARY (11th ed. 2019) (explaining the classic concept of judicial economy).

291. See Levy, *supra* note 290, at 445 (“[I]n a time of scarcity, certain cases should receive less judicial attention in the form of nontraditional review.”).

292. This is consistent with the original purpose of the trustee program. H.R. REP. NO. 95-595, at 4 (1977) (“The bill removes many of the supervisory functions from the judge in the first instance, transfers most of them to the trustee and to the United States trustee, and involves the judge only when a dispute arises. Because the judge no longer will have to take an active role in managing bankruptcy cases, the bankruptcy court should become a forum that is fair in fact and in appearance as well.”).

done by trustees in consumer versus business cases, and the reduced judicial oversight trustees receive in consumer cases all militate against the entangled status quo.

To avoid the inefficient and inequitable distortions created by the status quo, this Note has argued that Congress should create different compensation schemes tailored to the needs and realities of consumer and business bankruptcy. This Note has also argued that, to the same end, USTs should require Chapter 7 trustees to specialize. Either solution, or both, would help bring Chapter 7 in line with the rest of bankruptcy law and ensure a more efficient, fairer system for all debtors. Myriad improvements might be made in the future to Chapter 7, but disentangling its trustee system is a precondition for all of them.