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DISPLACING THE DEBTOR IN POSSESSION: THE REQUISITES FOR AND ADVANTAGES OF THE APPOINTMENT OF A TRUSTEE IN CHAPTER 11 PROCEEDINGS

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One of the most significant changes effected by the Bankruptcy Reform Act of 19781 (Code) involved the consolidation2 of Chapters X (Corporate Reorganization), XI

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2. The synthesis of Chapters X, XI and XII of the Act into an integrated Chapter 11 reflects the important and underlying input of the Commission on Bankruptcy Laws of the United States (Commission). The movement for comprehensive reform of the bankruptcy laws can easily be traced to Senator Quentin Burdick’s proposal to create the Commission. The original resolution, S.J. Res. No. 100, 90th Cong., 1st Sess. (1967), was introduced on August 2, 1967. The resolution creating the Commission was finally adopted on July 24, 1970, and the Commission was formed to “study, analyze, evaluate, and recommend changes” in the Bankruptcy Act. Act of July 24, 1970, Pub. L. No. 91-354, 84 Stat. 468. After several years of intensive study and hearings, the Commission issued its two-part report in July, 1973, REPORT OF THE COMMISSION ON THE BANKRUPTCY LAWS OF THE UNITED STATES, H.R. Doc. No. 137, 93d Cong., 1st Sess. (1973) [hereinafter cited as COMMISSION REPORT]. The first part of the COMMISSION REPORT contained the recommendations and findings of the Commission, while the second part consisted of the text of a proposed bankruptcy code [hereinafter cited as COMMISSION BILL], which was later introduced as H.R. 10792 and as S. 2565 in the 93d Congress, 1st Sess. (1973), and as H.R. 31 and S. 236 in the 94th Congress, 1st Sess. (1975).

The specific recommendation to consolidate the rehabilitation chapters of the Act was rooted in the Commission’s concern that, because there were no bright line standards to differentiate Chapter X from Chapter XI, the existence of several chapters for reorganization merely frustrated the rehabilitation process by involving the parties in collateral battles, most notably the costly and time consuming litigation over motions to convert the Chapter XI case to one under Chapter X. See COMMISSION REPORT, supra, at 241-48. See also Molle & Foltz, Chapter 11 of the 1978 Bankruptcy
(Arrangements), and XII (Real Property Arrangements) of the Bankruptcy Act (Act). In sweeping fashion, Congress created a unified reorganization chapter that is fundamentally grounded in the presumption that pre-bankruptcy management will continue to operate the business following the filing of a petition for relief. Concomitantly, however, Congress legislatively recognized the need for displacing the dishonest or grossly incompetent debtor in possession by creating a mechanism by which interested parties could seek the appointment of a trustee. In a very real sense, therefore, the Bankruptcy Code creates an inherent tension between the debtor who desires to remain in possession of its business and the creditor or other interested party who seeks to supplant the current management of the failing concern with a disinterested trustee.

The resolution of this tension presents interesting and sometimes conflicting questions of legislative history and

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The subsequent House Report accompanying H.R. 8200 criticized the divergent practices under Chapters X, XI and XII in even stronger terms, characterizing the distinctions between the chapters as "irrational" and stressing the need for a "flexible," consolidated reorganization chapter. H.R. Rep. No. 595, 95th Cong., Sess. 221-24 (1977), reprinted in 1978 U.S. Code Cong. & Ad. News 5963, 6180-83 [hereinafter cited as HOUSE REPORT]. Thus, the Bankruptcy Code, as enacted, reflects a significant departure from prior practice in the way that it consolidates the provisions dealing with reorganization.


4. The very structure of Chapter 11 dictates this conclusion in the way that sections 1108 and 1107 interrelate. Section 1108 provides that, unless the court orders otherwise, the trustee may operate the business. Section 1107, in turn, vests the debtor in possession with all the rights and powers of a trustee. See generally In re Curlew Valley Assocs., 14 Bankr. 506, 509-11 (Bankr. D. Utah 1981) (Judge Mabey provides an excellent analysis).

5. The mechanism is found in 11 U.S.C. § 1104(a) (1982).

6. One commentator has suggested that, because of the inherently adversarial nature of proceedings involving the displacement of current management, the trustee appointing mechanism in Chapter 11 has failed, partly because the adversary process itself does not create enough incentives to creditors to oppose the continued operation of the business by the debtor in possession. See LoPucki, The Debtor in Full Control—Systems Failure Under Chapter 11 of the Bankruptcy Code? (First Installment), 57 AM. BANKR. L.J. 99, 114 (1983).

7. See infra notes 14-49 and accompanying text.
judicial construction,8 ultimately calling for the balancing of competing reorganization policies.9 Section 1104(a) of the Bankruptcy Code effectuates this balance. Although much has been written about the operation of the Bankruptcy Code, very little has been said about the appropriate parameters of section 1104(a) of the Bankruptcy Code10 and the potential use of that provision to displace the overreaching debtor in full control.

8. See infra notes 52-109 and accompanying text.
9. See infra Part III and accompanying notes.
This article will examine the dimensions of section 1104(a) of the Bankruptcy Code. After exploring the legislative history of that Code provision and briefly contrasting the former practice under the Act, the article will trace the emerging judicial construction of the operative language in section 1104(a), focusing upon the use of a motion for the appointment of a trustee as an important arrow in the creditor's quiver of rights. Finally, the article will outline the advantages in seeking the appointment of a trustee.

I. LEGISLATIVE HISTORY AND BACKGROUND

Section 1104(a) of the Bankruptcy Code provides, in pertinent part:

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

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

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

As enacted, section 1104 "represents a compromise between the House bill and the Senate amendment concern-

11. See infra note 25 and accompanying text.
12. See infra notes 52-109 and accompanying text.
14. The House bill referred to in this passage is H.R. 8200, 95th Cong., 1st Sess. (1977), which was originally introduced by members of the Subcommittee on Civil and Constitutional Rights of the House Committee on the Judiciary on July 11, 1977. See generally Klee, supra note 1, at 281-82.
15. The Senate amendment referred to in this passage is the Senate version of H.R. 8200. Consistent with normal Senate parliamentary procedure, after the Senate considered the House version of H.R. 8200, the Senate struck the entire text of H.R. 8200, save for the enacting clause, and inserted the text of S. 2266, 95th Cong., 2d Sess. (1978), as amended, which was the Senate bill. Thus, the Senate amendment simply refers to the Senate version of H.R. 8200, and is perhaps more accurately
ing the appointment of a trustee or examiner.16 Notwithstanding this deceptively simple statement, the legislative history of section 1104(a) is marked by strong clashes of opinion and policy, causing at least one noted textwriter to observe that "very few issues dealt with by Congress in connection with the drafting of the Code produced a greater divergence of views than the standards for the appointment of trustees."17 Congress struggled over numerous issues, including whether to require the appointment of a trustee in every case,18 and whether the relative size of a debtor corpo-

described as the "Senate amendment in the nature of a substitute to H.R. 8200." Klee, supra note 1, at 288-89.


18. The House and Senate Reports dealing with the narrow issue of whether to appoint a trustee in every case graphically illustrate the extent to which the leading proponents of the Bankruptcy Code differed. The House Report favored a flexible approach that did not require the appointment of a trustee in every reorganization case, citing the abuses engendered by the then existing Chapter X and Chapter XI schema. See House Report, supra note 2, at 104, 232-34 and 402-03, reprinted in 1978 U.S. CODE CONG. & AD. NEWS 6065-66, 6191-94, 6357-59. Rather, the House version of the Bankruptcy Code required the bankruptcy court to consider the appointment of a trustee on a case-by-case basis. Id. In contrast, the Senate Report accompanying the original Senate version of the Bankruptcy Code, S. 2266, mirrored the concerns of the Securities and Exchange Commission, and favored the mandatory appointment of a disinterested trustee in cases involving a "public company." S. REP. No. 989, 95th Cong., 2d Sess. 1, 9-11, reprinted in 1978 U.S. CODE CONG. & AD. NEWS 5787, 5795-97 [hereinafter cited as SENATE REPORT]. A "public company" was defined to mean "a debtor who, within 12 months prior to the filing of a petition for relief under this chapter, had outstanding liabilities of $5 million or more, . . . and not less than 1,000 security holders." S. REP. No. 95-598, 95th Cong., 2d Sess. 9-11, 115, reprinted in 1978 U.S. CODE CONG. & AD. NEWS 5787, 5795-97, 5901. See also Levy, The Role of the Securities and Exchange Commission and the Judicial Functions Under the Bankruptcy Reform Act of 1978, 54 AM. BANKR. L.J. 29, 29-34 (1980). The
ration or the fact that it is publicly owned is relevant to the determination of whether "cause" exists to appoint a trustee.19 Ultimately, Congress opted for an admixture of the House and Senate versions of the Bankruptcy Code in that “[t]he method of appointment rather than election, is derived from the House bill; [and] the two alternative standards of appointment are derived with modifications from the Senate amendment, instead of the standard stated in the House bill.”20

Because neither the House Report21 nor the Senate Report22 deal with versions of section 1104(a) that were actually enacted into law, it is all the more important to understand the contextual development of section 1104(a).23

provisions requiring mandatory appointment of trustees contained in the Senate version of the bill were deleted from the final version of the Bankruptcy Code. See 124 Cong. Rec. 33,990, 34,004-05 (1978).


The only remnant of the “public company” concept is now found in the provisions governing the appointment of an examiner. 11 U.S.C. § 1104(b) (1982). Reflecting the compromise which occurred between the terms of the final House bill, which provided that an examiner would be appointed only if the protection of a trustee was needed and the costs and expenses were not disproportionately high, and the terms of the final Senate bill, which required the appointment of a trustee in the case of a “public company” and permitted the appointment of an examiner in the case of non-public company if the appointment would serve the interest of the state and security holders, section 1104(b), as enacted, provides that an examiner must be appointed if “the debtor's fixed, liquidated, unsecured debts, other than debts for goods, services, or taxes, or owing to an insider, exceed $5,000,000.” 11 U.S.C. § 1104(b)(2). Compare the final House Bill, H.R. 8200, 95th Cong., 1st Sess. § 1104 (1977), with the final Senate Bill, S. 2266, 95th Cong., 2d Sess. § 1101(3) (1978) (defining Public Companies). Compare also House Report, supra note 2, at 402-03, 1978 U.S. Code Cong. & Ad. News at 6358-59, with Senate Report, supra note 18, at 115, 1978 U.S. Code Cong. & Ad. News at 5901. See generally Hughes, supra note 10, at 52-55.

20. 124 Cong. Rec. 32,405, 34,005 (1978); see also supra note 16 and accompanying text.

21. See supra note 2.

22. See supra note 18.

23. Numerous courts have astutely observed that, because both the House and Senate Reports dealt with versions of section 1104(a) that were not enacted into law, there is very little relevant legislative history on section 1104(a). See, e.g., Flushing
Like many other provisions of the Bankruptcy Code, the mechanism providing for the appointment of a trustee in a Chapter 11 case is deeply rooted in the recommendations, findings and proposal of the Commission on the Bankruptcy Laws of the United States.24 Dissatisfied with the uneven and often arbitrary approach to the appointment of trustees under the Act,25 the Commission recommended that the ap-

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24. See generally supra note 2. The Commission consisted of nine members: three appointed by the President and two each by and from the Senate, House and Judiciary. The Presidential appointees were Harold Marsh, Jr., J. Wilson Newman and Professor Charles Seligson. Senators Quentin N. Burdick and Marlow W. Cook were appointed by the President of the Senate. Representatives Don Edwards and Charles E. Wiggins were appointed by the Speaker of the House, and District Judges Edward Weinfeld and Hubert L. Will were appointed by the Chief Justice. Professor Frank R. Kennedy served as executive director of the Commission.

25. See generally supra note 2. The Commission was troubled by the way the structure of the reorganization chapters under the Act contributed to costly and time-consuming litigation, often because a putative debtor sought mightily to avoid being automatically displaced by the requisite appointment of a trustee under Chapter X. See COMMISSION REPORT, supra note 2, at 241-48. The Commission found that the rehabilitation chapters of the Act have "detailed and overlapping rules regarding [their] availability which frequently produce pointless and wasteful litigation as to which chapter should be utilized in a particular case . . . . In addition, none of the chapters is precisely suited to the needs of many common business situations." COMMISSION REPORT, supra note 2, at 23.

To understand the basis for the Commission's concerns more fully, it may be helpful to digress briefly by juxtaposing the former practice under the Act. Under Chapter X of the Act, the bankruptcy court was required to appoint a trustee in every case where the debtor's noncontingent, liquidated liabilities exceeded $250,000. Bankruptcy Act ch. 575, § 156, 52 Stat. 888 (1938) (former 11 U.S.C. § 556 (1976) (repealed 1978)). Former Fed. Bankr. R. 10-202(a) (1973) also permitted the court to appoint a trustee on application, and for cause. See Fed. Bankr. R. 11-18(b) (1973).
pointment of an independent trustee be discretionary except in cases where the debtor is a corporation with debts of $1,000,000 or more and 300 or more security holders. In this case the appointment of a trustee would be presumptive, absent a finding by the bankruptcy court that the protection afforded by a trustee is unnecessary or that the expense incurred by the appointment of a trustee would be disproportionate to the protection afforded. 26 Although still considerably deferential to the views of the Securities and Exchange Commission (SEC), 27 the Commission's proposal was, nevertheless, a substantial step forward over prior prac-

More importantly, section 328 of Chapter XI (added July 7, 1952, ch. 579, § 30, 66 Stat. 432 (11 U.S.C. § 782 (1976)) and Fed. Bankr. R. 11-15 (1973) permitted the Securities and Exchange Commission (SEC), or other party in interest, to move to convert the proceedings to a case under Chapter X of the Act. Thus, the rehabilitation effort was often delayed by prolonged litigation over the issue of whether the debtor was a proper candidate for Chapter XI. See, e.g., Securities & Exch. Comm'n v. American Trailer Rentals Co., 379 U.S. 594 (1965); General Stores Corp. v. Shlensky, 350 U.S. 462 (1956); Securities & Exch. Comm'n v. United States Realty & Improvement Co., 310 U.S. 434 (1940); Securities & Exch. Comm'n v. Canandaigua Enter. Corp., 339 F.2d 14, 19 (2d Cir. 1964) (commenting that the Chapter XI and Chapter X schema produces pointless and wasteful litigation as to which Chapter should be utilized with the resulting risk that "the patient may die before an operating room is ready or for which the fees of the surgeon and others in attendance may exceed the patient's means.").

Finally, Chapter XII left the debtor in possession in nearly all cases, except where a trustee was appointed under a prior filing under another chapter or where, for cause shown, the court appointed a trustee. Bankruptcy Act § 432, ch. 575, 52 Stat. 918 (11 U.S.C. § 832 (1976) (repealed 1978)), and Fed. Bankr. R. 12-17(a) and (b)).

Thus, under the former practice, the issue of whether or not debtor's management should be replaced by an independent trustee was largely dependent upon the choice of the rehabilitation chapter, and not necessarily the needs of the case.

26. COMMISSION REPORT, supra note 2, at 253. The specific Commission recommendation was contained in section 7-102 of the proposed Bankruptcy Act of 1973, which provided, in pertinent part, that:

(a) Determination by Court. On the application of the administrator or any party in interest, and after hearing on notice, the court may order the administrator to appoint a trustee. If the debtor is a corporation having debts of $1,000,000 or more and 300 or more security holders, the administrator shall apply to the court to determine whether a trustee should be appointed, and the court shall order such appointment unless it finds that the protection afforded by a trustee is unnecessary or that the expense would be disproportionate to the protection afforded.

Id. at 221. The Commission's proposed legislation was introduced in the 93d Cong. as H.R. 10792, 93d Cong., 1st Sess. (1973) and S. 2565, 93 Cong., 1st Sess. (1973). See supra note 2.

tice in that it provided for a more flexible, discretionary approach to the displacement of current management. 28

Shortly after the Commission's proposal was released, the National Conference of Bankruptcy Judges drafted and submitted an alternative Bankruptcy Act. 29 Although the Commission's and Bankruptcy Judges' proposals differed in many respects, the Judges' recommendation with respect to the appointment of a trustee was almost identical to the Commission's proposal. 30 Not surprisingly, the SEC voiced strong opposition to many of the changes recommended by the Commission and the National Conference of Bankruptcy Judges. The SEC particularly opposed the proposed elimination of the mandatory appointment of disinterested trustees for public companies. 31 The SEC complained that,
in large public cases, the investors' interests would not be adequately protected because the proposed legislation created unworkable delays, aggravated the transitional problems and trauma occasioned by the mere filing of a bankruptcy petition, and, in general, failed to recognize the advantages of a disinterested trustee. Accordingly, the SEC proposed textual changes deleting those sections of the Commission's and Judges' bills pertaining to the discretionary appointment of a trustee, and inserting instead a provision modeled after section 156 of Chapter X of the Bankruptcy Act, which called for the mandatory, immediate appointment of a trustee.

Although Congress ultimately rejected the SEC's proposed "mandatory appointment rule" in large public cases, it is clear that the SEC's input had an immediate and decisive impact upon the legislative history of section 1104(a). In the two years which followed, the sharply divergent views concerning the standards for the appointment of a trustee in a Chapter 11 proceeding crystallized into two different congressional bills, House bill 8200 and Senate bill 2266.

709, 715 (testimony and statements of then SEC Commissioner Philip A. Loomis, Jr.); HEARINGS ON H.R. 31 AND H.R. 32, supra note 17, at 2164-2210 (especially 2175-80) (Report of Securities and Exchange Commission on Proposed Bankruptcy Legislation (H.R. 31 and H.R. 32)); id. at 2152-54 (statement of then SEC Commissioner Philip A. Loomis, Jr.).


33. See id. at 2162 (statement of then SEC Commissioner Philip A. Loomis, Jr.).

34. See supra note 18.

35. H.R. 8200, 95th Cong., 1st Sess. (1977). H.R. 8200 was the product of many compromises, evolving from H.R. 6, which was introduced by Representatives Don Edwards and M. Caldwell Butler on January 4, 1977. H.R. 6, 95th Cong., 1st Sess. (1977); H.R. 6 represented a merger of the Commission's and Judges' bills, together with the input of numerous other interested organizations and individuals, most notably the National Bankruptcy Conference. See Klee, supra note 1, at 280. H.R. 6 was replaced by H.R. 7330 on May 23, 1977, following extensive revisions and amendments during markup. H.R. 7330, 95th Cong., 1st Sess. (1977); Klee, supra note 1, at 281. After additional markup, H.R. 7330 was superseded by H.R. 8200, which was reported on July 11, 1977, with strong support by the House Judiciary Committee. Following additional discussion and circulation, H.R. 8200 passed the House by voice vote on February 1, 1978. 124 Cong. Rec. 1783 (1978); Klee, supra note 1, at 282, 287.

36. S. 2266, 95th Cong., 2d Sess. (1978). S. 2266 was "essentially the analogue of H.R. 8200, although there were substantial differences between the two bills." Klee, supra note 1, at 285. S. 2266 was introduced in the Senate on October 31, 1977, by
House bill 8200 largely mirrored the Commission's and Bankruptcy Judges' proposals by requiring the bankruptcy court to determine on a case-by-case basis, whether the appointment of a trustee is necessary taking into account whether the costs and expenses outweigh the benefits provided to the estate.\textsuperscript{37} Senate Bill 2266, on the other hand, altered the Commission's and Bankruptcy Judges' proposals and acquiesced, at least in part, in the SEC's proposal by mandating the appointment of a trustee\textsuperscript{38} in any case involving a so-called "public company,"\textsuperscript{39} but otherwise permitting the discretionary appointment of a trustee in "nonpublic" cases.\textsuperscript{40} Not surprisingly, the SEC strongly endorsed the Senate's version of section 1104(a), testifying that the Senate's alternative would overcome the weaknesses of both

\textsuperscript{37} Section 1104(a) of H.R. 8200 provided that:

\begin{quote}
At any time after the commencement of the case but before the confirmation of a plan, on request of a party in interest or the United States trustee, and after notice and a hearing, the court may order the appointment of a trustee only if—

1. the protection afforded by a trustee is needed; and
2. the costs and expenses of a trustee would not be disproportionately higher than the value of the protection afforded.
\end{quote}

\textsuperscript{38} Section 1104(a) of S. 2266 provided in pertinent part, that: "In the case of a public company, the court, within ten days after entry of an order for relief under this chapter, shall appoint a disinterested trustee."

\textsuperscript{39} S. 2266, § 1101(3). See also supra notes 18-19 and accompanying text.

\textsuperscript{40} Section 1104(b) of S. 2266 essentially followed the House formulation of section 1104(a). For convenience in comparing H.R. 8200 and S. 2266, the provisions in H.R. 8200 deleted from S. 2266 are enclosed in brackets, and the new material in S. 2266 is printed in italic.

\begin{quote}
\textit{In the case of the nonpublic company, at any time after the commencement of the case but before the confirmation of a plan, on request of a party in interest [or the United States trustee,] and after notice and a hearing the court for cause shown may order the election or if the creditors do not elect a trustee the court may appoint a trustee. The court shall order the election or if the creditors do not elect appointment of a trustee [only] if—

1. the protection afforded by a trustee is needed; and
2. the costs and expenses of a trustee would not be disproportionately greater than the value of the protection afforded.}
\end{quote}
House Bill 8200 and the related proposals of the Commission and the Bankruptcy Judges. 41

Notwithstanding the sharply critical views of the SEC, however, the final congressional product largely reflects the House view on the appointment of trustees. 42 With the exception of the Code provision requiring the appointment of an examiner where the debtor's liabilities exceed $5,000,000 and a party in interest requests such an appointment, 43 there are no other "remnant[s] of the 'public company' exception contained in S. 2266." 44 Yet, while section 1104(a) of the Bankruptcy Code "is derived in large part" from the version of Chapter 11 contained in the House bill, 45 and "rejects the


42. As much as anything else, Pub. L. 95-598, as enacted, is witness to a concerted effort by the House and Senate managers of H.R. 8200 and S. 2266 to produce a compromise. Nevertheless, "[s]ince the Senate view prevailed on the question of the status of the bankruptcy courts and the House view prevailed on business reorganizations, it is somewhat tempting to look at this final compromise as a quid pro quo involving these two aspects of the proposed Code." Securities and Exchange Commission, The Securities and Exchange Commission's Role in Bankruptcy Reorganization Proceedings, A Report by Commissioner Bevis Longstreth (November 21, 1983) at 49, Exhibit B, General Counsel's Memorandum [hereinafter cited as Longstreth Report and General Counsel's Memorandum, respectively]. The General Counsel's Memorandum, entitled "The Role of the Securities and Exchange Commission in Bankruptcy Reorganization Cases," and dated September, 1983, was prepared by the Office of the General Counsel of the Securities and Exchange Commission at the request of Commissioner Longstreth in connection with the Commissioner's broader examination of the presence of the Securities and Exchange Commission in bankruptcy proceedings. The General Counsel's Memorandum is divided into two parts. Part I consists of a legal analysis of the SEC role in bankruptcy reorganization cases, while Part II largely consists of a statistical analysis of the SEC practice under the new Bankruptcy Code in bankruptcy court, including a case profile and issue analysis of the success of the SEC.


44. 5 Collier on Bankruptcy, supra note 10, ¶ 1104.02, at 1104-28.

45. 124 Cong. Rec. 32,403 (1978) (floor statement of Representative Don Edwards on the passage of the House amendment to the Senate amendment in the nature of a substitute to H.R. 8200); 124 Cong. Rec. 34,003 (1978) (floor statement of Senator Dennis DeConcini on the passage of the final Senate amendment in the nature of a substitute to H.R. 8200).
concept of separate treatment for a public company,"46 neither the courts47 nor the commentators48 have ignored the fact that "the two alternative standards of appointment are derived with modifications from the Senate amendment, instead of the standard stated in the House bill."49 Thus, Part II of this article examines how the courts have construed section 1104(a) in light of its unusual legislative history.

II. JUDICIAL CONSTRUCTION AND ANALYSIS OF SECTION 1104(A)

Because both the structure50 and the legislative history51 of Chapter 11 evidence a clear intent on the part of Congress to allow the debtor to remain in possession, the courts have exhibited an understandable reluctance to appoint trustees. The authorities are in agreement that the moving52 party

47. See infra text accompanying notes 59-60.
48. See, e.g., Moller, supra note 10, at 460-61; Moller & Foltz, supra note 2, at 910 (arguing that because section 1104(a) embodies the same criteria previously relied upon by the SEC in its motion practice under section 328 of the Act and Federal Bankruptcy Rule 11-15, section 1104(a) merely effects a "renaming" of an old motion).
50. The interplay between sections 1106, 1107, 1108, 363(c)(1) and 303(f) makes it clear that, unless the court orders otherwise, the debtor continues to operate the business once a petition, even an involuntary petition, is filed. See generally 11 U.S.C. §§ 303(f), 363(c)(1), 1106-1108 (1982). Under the Bankruptcy Code, the debtor in possession has all the rights and powers of a trustee under section 1107(a), and the reference to "trustee" in section 1108 includes the debtor in possession. See also supra note 4 and case cited therein.
51. See, e.g., House Report, supra note 2, at 404, reprinted in 1978 U.S. CODE CONG. & AD. NEWS at 6360; Senate Report, supra note 18, at 116, reprinted in 1978 U.S. CODE CONG. & AD. NEWS at 5902; see also 124 Cong. Rec. 32,405, 34,005 (1978) ("section 1107 applies to give the debtor in possession all the rights and powers of a trustee in a case under Chapter 11; this includes the power of the trustee to operate the debtor's business under section 1108.").
52. As noted above, a trustee is appointed only at the request of a party in interest and "after notice and a hearing." 11 U.S.C. § 1104(a) (1982). The phrase "after notice and a hearing" is defined in section 102(1)(A) to mean "after such notice as is appropriate in the particular circumstances, and such opportunity for a hearing as is appropriate in the particular circumstances . . . ." 11 U.S.C. § 102(1)(A) (1982). In this regard, BANKR. R.P. 9007 provides that, when notice is to be given, as it must when a party seeks the appointment of a trustee, the bankruptcy court "shall designate . . . the time within which, the persons to whom, and the form and manner in which the notice shall be given."

It appears that the Bankruptcy Code and the newly adopted Bankruptcy Rules contemplate that a party seeking the appointment of a trustee should do so by filing a
bears a heavy burden in overcoming the presumption that the debtor should remain in possession. The courts frequently note that, although perhaps not a disfavored remedy, a motion for the appointment of a trustee should at least

motion. The necessity of filing a motion to appoint a trustee arises by negative implication. Bankr. R.P. 7001, which defines those proceedings which are treated as "adversary proceedings" for purposes of the Bankruptcy Rules, does not include the appointment of a trustee among its list of ten items which are governed by Part VII of the Bankruptcy Rules. Accordingly, the inference arises that a party seeking the appointment of a trustee should treat the matter as a "contested matter" under Rule 9014, and file and serve a motion for the appointment of a trustee (or, in the alternative, for an examiner) pursuant to Rule 9013. As a practical matter, however, this may prove to be a difference without anything more than a $60.00 distinction since a contested motion seeking the appointment of a trustee is likely to put the case in an extremely adversarial posture, particularly since the moving party will probably wish to obtain a scheduling order providing for expedited discovery and a hearing on a fairly short-term basis.

It should also be noted that section 102(1)(B) authorizes the court to act without an actual hearing if the moving party does provide proper notice and if "such a hearing is not requested timely by a party in interest" or "there is insufficient time for a hearing to be commenced before such act must be done, and the court authorizes such act . . . ." 11 U.S.C. § 102(1)(B)(i)-(ii) (1982). Although it is unlikely that any court would invoke such an extraordinary remedy without an opportunity for the debtor to be heard, the facts and circumstances of the case may dictate such a result, particularly where the debtor's conduct is so flagrantly fraudulent or dishonest as to mandate the immediate displacement of current management. See In re Consolidated Equities, Inc., No. 84-0466 slip. op. (D.P.R. March 6, 1984) (available Jan. 2, 1984, on LEXIS, Bkrtcy library) ("Hearings on motions for appointment of trustees are not among the events for which Bankruptcy Rule 2002(a) requires not less than a twenty-day notice to the debtor.").
be considered an extraordinary remedy, and one which may impose a substantial financial burden on the already hard-pressed debtor seeking relief under the Bankruptcy Code.\(^5\)

The evolving case law under section 1104(a) of the Bankruptcy Code closely reflects both the pattern of analysis suggested by the relevant legislative history of the final congressional product and the "fresh start" policy which underlies much of the Bankruptcy Code.\(^5\) The courts have recognized that some evidence of mismanagement, imprudent decision making, and lack of "exemplary business acumen"\(^5\) is to be expected, and, accordingly, merely establishing that the debtor exercised poor business planning will not suffice to overcome the presumption that the debtor shall remain in possession.\(^5\)


\(^{55}\) See, e.g., House REPORT, supra note 2, at 220, reprinted in 1978 U.S. Code Cong. & Ad. News at 6179-80. See also 5 COLLIER ON BANKRUPTCY, supra note 10, at 1104.01, at 1104-21 ("The philosophy of Chapter 11 is to give the debtor a 'second chance'. . . .")

\(^{56}\) See generally 5 COLLIER ON BANKRUPTCY, supra note 10, at 1104-21.


In a related vein, the courts also properly observe that it is not the function of a bankruptcy court to second guess the debtor's business judgment unless that business judgment evidences gross incompetence or dishonesty. See, e.g., In re UNR Indus.,
Moreover, the courts are quick to draw a distinction between the kind of analysis dictated by section 1104(a)(1), the "for cause" standard, and the kind of analysis dictated by section 1104(a)(2), the "best interests" standard. More precisely, the better reasoned authorities note that, under the section 1104(a)(1) "for cause" standard, the courts' discretion is necessarily more circumspect because the literal language of the statute mandates the appointment of a trustee in those instances where the evidence satisfies the "for cause" standard. Not surprisingly, therefore, most courts that

Inc., 30 Bankr. 609, 612 (Bankr. N.D. Ill. 1983); In re Frank, 27 Bankr. 748, 750 (Bankr. S.D. Ohio 1983); Allied Technology, Inc. v. R.B. Brunemann & Sons, Inc. (In re Allied Technology, Inc.), 25 Bankr. 484, 495 (Bankr. S.D. Ohio 1982). See also In re Curlew Valley Assocs., 14 Bankr. 506, 511 (Bankr. D. Utah 1981) ("The courtroom is not a boardroom."). Significantly, it is not the quality of the debtor in possession's management that is the subject of review so much as it is the integrity of current management. As the bankruptcy court properly noted in Smith v. Concord Coal Corp. (In re Concord Coal Corp.), 11 Bankr. 552, 554 (Bankr. S.D.W. Va. 1981), the time for evaluating the quality of the debtor in possession's management is at the time of confirmation pursuant to the dictates of section 1129(a)(5)(A)(i)-(ii).

58. As noted by Bankruptcy Judge Watson in his excellent analysis in In re Anniston Food-Rite, Inc., 20 Bankr. 511, 514-15 (Bankr. N.D. Ala. 1982), the fact that section 1104(a) has two alternative standards was no Congressional accident, although the "for cause" and "best interests" standards were once conjunctive tests in the House bill. See HOUSE REPORT, supra note 2, at 402, 1978 U.S. CODE CONG. & AD. NEWS 6357. See also infra note 78. Nevertheless, the final legislative enactment clearly shows that Congress deliberately disjoined the two tests, choosing instead to create two separate bases for the appointment of a trustee. In re Anniston Food-Rite, Inc., 20 Bankr. 511, 514-15 (Bankr. N.D. Ala. 1982). See also In re Garland Corp., 6 Bankr. 456, 460 (Bankr. 1st Cir. 1980).

The disjunctive nature of these two tests has caused some degree of consternation because it is difficult to imagine a situation where a court would find that "cause" existed to appoint a trustee but that such an appointment was not in the "best interests" of the creditors and equity security holders. See, e.g., Anniston Food-Rite, Inc., 20 Bankr. at 515; 5 COLLIERS ON BANKRUPTCY, supra note 10, ¶ 1104.01, at 1104-21 to -23. Conversely, it would be difficult to imagine a situation that satisfied the "best interests" standard that did not also satisfy the requisites of the "for cause" standard. Nevertheless, a number of courts have found that evidence which was insufficient to satisfy the "for cause" standard was sufficient to permit the appointment of trustee under the "best interests" standard. See generally infra notes 94-103 and accompanying text.

have carefully examined the “for cause” standard require the moving party to establish the requisite “cause” by clear and convincing evidence.60

In contrast, the judicial construction of the section 1104(a)(2) “best interests” standard has emphasized the courts’ “broad equity powers to engage in a cost-benefit analysis in order to determine whether the appointment of a trustee would be in the interests of creditors, equity security holders, and other interests of the estate.”61 Typically, the courts note that section 1104(a)(2) embodies a more flexible standard under which the bankruptcy court can more readily exercise its historically broad equitable powers.62 The courts have also observed that a moving party should not confuse its own self interest with the interests of the estate and credi-

Bankr. 169, 174 (Bankr. N.D. Ga. 1980). See also Flushing Sav. Bank v. Parr (In re Parr), 1 Bankr. 453, 457 (Bankr. E.D.N.Y. 1979) (“While rejecting the Senate version, which would have made the appointment of a trustee mandatory in the case of a public company, § 1104(a) as enacted, unlike the House version, does make it mandatory for the Bankruptcy Court to appoint a trustee if the requirements of subdivision (1) . . . are met.”). Also note Judge Schwartzberg’s careful explication of the legislative history surrounding the use of the word “shall” in section 1104(a)(1) in In re McCordi Corp., 6 Bankr. 172, 176-78 (Bankr. S.D.N.Y. 1980).

But see Official Creditors’ Comm. v. Liberal Mkt., Inc. (In re Liberal Mkt., Inc.), 13 Bankr. 748, 751 (Bankr. S.D. Ohio 1981), and In re Main Line Motors, Inc., 9 Bankr. 782, 784 (Bankr. E.D. Pa. 1981), in which the bankruptcy courts suggest that the equitable considerations dictated under the section 1104(a)(2) “best interests” analysis are also applicable to a determination of whether a trustee should be appointed “for cause” under section 1104(a)(1). Compare these with Bankruptcy Judge Watson’s criticism of Main Line Motors in In re Anniston Food-Rite, Inc., 20 Bankr. 511, 516 (Bankr. N.D. Ala. 1982).


tors generally,63 and that, notwithstanding the Congressional intent to weigh the costs of appointing a trustee against the concomitant benefits,64 the "cost-benefit" factor must ultimately give way to the "cost-protection" factor, even at the risk of depleting the estate.65

While it is clear that section 1104(a) empowers the court to exercise its broad equitable discretion on a case-by-case basis, it is also clear that Congress carefully delimited the scope of the bankruptcy court’s equitable powers. For example, although the Bankruptcy Code provides that the bankruptcy court may issue any order, process or judgment necessary to carry out the provisions of the Code,66 the court is expressly prohibited from appointing a receiver.67 The appointment of a trustee is the only statutorily authorized alternative to a debtor in possession in Chapter 11 proceedings.68 Moreover, because the court itself is not a "party in interest," it may not, on its own motion, order the appointment of a trustee under section 1104.69 Thus, the

64. See, e.g., HOUSE REPORT, supra note 2, at 402-03, reprinted in 1978 U.S. CODE CONG. & AD. NEWS 6357-58.
67. 11 U.S.C. § 105(b) (Supp. III 1979). One of the purposes of section 105(b) is to prevent a bankruptcy court from appointing a receiver where no grounds exist for the appointment of a trustee under section 1104(a). 5 COLLIER ON BANKRUPTCY, supra note 10, ¶ 1104.01, at 1104-22 n.45. See also SENATE REPORT, supra note 18, at 29, reprinted in 1978 U.S. CODE CONG. & AD. NEWS at 5815. But cf. In re Record & Tape Place, Inc., No. 81-1665-L, (Bankr. D. Mass. April 7, 1983) (available Apr. 26, 1984, on LEXIS, Bkrtcy library) (after properly noting that the prior confirmation of the debtor's plan effectively cut off the court's authority to appoint a trustee, the court nevertheless appointed a "supervisor" pursuant to 11 U.S.C. § 105(a) (1982) to monitor and investigate the postconfirmation operations of the debtor).
68. In re Casco Bay Lines, Inc., 17 Bankr. 946, 952 (Bankr. 1st Cir. 1982). As the Casco Bay Lines appellate panel noted, a Chapter 11 reorganization envisions only two possible alternatives: the debtor in possession or the debtor "out of possession," the latter instance of which mandates the appointment of a trustee. Id. at 951.
69. The literal language of section 1104(a) restricts the discretion of the court in that a trustee may only be appointed on request of a party in interest and after notice and a hearing. The phrase "party in interest" is defined in section 1109(b) in such a way as to make it clear that the court may not, sua sponte, raise the issue of the need for the appointment of a trustee. 11 U.S.C. § 1109(b) (1982). See also In re Mandalay Shores Co-op. Housing Ass'n, 22 Bankr. 202, 207 (Bankr. M.D. Fla. 1982); In re Harper Indus., Inc., 18 Bankr. 773, 775 (Bankr. S.D. Ohio 1982); In re Alpine Lumber & Nursery, 13 Bankr. 977, 979 (Bankr. S.D. Cal. 1981); In re Gurwitch, 6 BANKR. Ct.
burden of displacing the debtor in possession falls squarely upon the moving party.

A. Appointment of a Trustee "For Cause"

Having outlined the general parameters of the emerging judicial construction of section 1104(a), the discussion now turns to a more specific analysis of the two alternative standards, beginning with the "for cause" standard embodied in section 1104(a)(1). Pursuant to section 1104(a)(1), and in pilot districts:\textsuperscript{70} pursuant to section 151104(a),\textsuperscript{71} a party in interest may seek the appointment of a trustee "for cause," including fraud, dishonesty, incompetence, or gross misman-
agement of the affairs of the debtor by current management, either before or after the commencement of the case. The grounds listed in section 1104(a)(1) are not exclusive, and it is arguable that "cause" also includes at least some of the

1981). Moreover, the trustee or examiner to be appointed in the case must be disinterested, and cannot be the United States Trustee. 11 U.S.C. § 151104(c) (1982).

The United States Pilot Program has proven to be immensely successful. Based upon a highly favorable evaluation of the program by Abt Associates of Cambridge, Massachusetts, it is anticipated that the Reagan administration will recommend an extension of the program through September, 1986, and an increase in its annual budget for fiscal year 1984 to about $8,200,000. Longstreth Report, supra note 42, at 4. Indeed, although the program was scheduled to "sunset" as of March 30, 1984, section 408(c) of Pub. L. 95-598 was recently amended by Act of Nov. 28, 1983, Pub. L. 98-166, 97 Stat. 1081 [hereinafter cited as Pub. L. No. 98-166], to extend the life of the United States Trustee system to September 30, 1984. Finally, the efficacy of the United States Trustee program is borne out by the fact that the SEC, obviously pleased with the performance of the United States Trustees, recently voted unanimously to accept the recommendation of the Longstreth Report to eliminate the SEC's active involvement in pilot districts except where specifically requested to act by the United States Trustee or the bankruptcy court. Longstreth Report, supra note 42, at 11-13.

Finally, it is extremely significant to note that the recently filed Report of the Attorney General on the United States Trustee System, required by section 408(b) of the Bankruptcy Reform Act, also concludes that the United States Trustee program has been immensely successful. U.S. Department of Justice (Office of the Attorney General), Report of the Attorney General on the United States Trustee System, Established in the Bankruptcy Reform Act of 1978, for the Period October 1, 1979 to December 31, 1983 (January 3, 1984) [hereinafter cited as Attorney General's Report]. Among other things, the Attorney General's Report highlights the role of United States Trustees in Chapter 11 cases, noting that "the Trustees have monitored and assisted in the cases that lack active creditor involvement." Id. at 54. The authors of the Attorney General's Report also believe that "the higher rate of plan confirmation and the lower rate of case inactivity in the pilot districts reflect, in part, the Trustees' contributions." Id. Based upon these and numerous other findings, the Attorney General's Report also recommends that the United States Trustee program be implemented on a nationwide basis. Id. at 61-66.


73. The rules of construction of the Bankruptcy Code make it clear that the words "includes" and "including" are not limiting. See 11 U.S.C. § 102(3) (1982). The courts have rejected any attempts to limit the "for cause" analysis under section 1104(a)(1) to cause "in the nature of fraud, dishonesty, incompetence or gross mismanagement." See, e.g., In re Casco Bay Lines, Inc., 17 Bankr. 946, 950 n.4 (Bankr. 1st Cir. 1982). See also In re Ford, 36 Bankr. 501, 504 (Bankr. W.D. Ky. 1983); In re Martin, 26 Bankr. 39, 40 (Bankr. S.D.W. Va. 1982).
grounds for conversion listed in section 1112(b) of the Bankruptcy Code.\textsuperscript{74}

The authorities are in agreement that the time frame for the court's review of current management's actions embraces conduct both before and after the commencement of the case.\textsuperscript{75} The courts have emphasized that neither prepetition repentance nor a postpetition change of heart of the debtor in possession will obviate the need for the appointment of a trustee,\textsuperscript{76} and that "self-serving testimony as to how past and current management intends to improve management and operational actions is mere speculation and not relevant to the issues of whether past management actions require the appointment of a trustee under \$1104(a)."\textsuperscript{77}

\textsuperscript{74} The only other provision of the Bankruptcy Code which employs the phrase "for cause" is section 1112(b), the provision governing conversion or dismissal of a case commenced under Chapter 11 of the Bankruptcy Code. Section 1112(b) lists nine examples of "cause" for conversion, all but the last four of which provide an arguable basis for seeking the appointment of a trustee. See, for example, \textit{In re} Horn & Hardart Baking Co., 22 Bankr. 668, 671 (Bankr. E.D. Pa. 1982), where the bankruptcy court appointed a trustee after the debtor in possession experienced continuing and unexplained losses since the filing of the petition. The last four grounds could not serve as the basis for the appointment of a trustee since section 1104(a), by its literal terms, precludes the court from appointing or considering the appointment of a trustee after the confirmation of a plan. See generally Note, The Misbehaving Debtor, supra note 10, at 478, 488 n.54.

\textsuperscript{75} See, e.g., \textit{In re} Anniston Food-Rite, Inc., 20 Bankr. 511, 515 (Bankr. N.D. Ala. 1982); \textit{In re} Curlew Valley Assocs., 14 Bankr. 506, 515 (Bankr. D. Utah 1981); Dardarian v. La Sherene, Inc. (\textit{In re} La Sherene, Inc.), 3 Bankr. 169, 175 (Bankr. N.D. Ga. 1980); see also \textit{In re} Main Line Motors, Inc., 9 Bankr. 782, 784-85 (Bankr. E.D. Pa. 1981) ("The fact that the events preceded the bankruptcy petition is not controlling because section 1104(a)(1) embraces activities 'either before or after the commencement of the case.'")

One leading textwriter has suggested that section 1104(a)(1) "does not permit the court to order the appointment of a trustee solely on the grounds that current management has mishandled the debtor's affairs." 5 \textit{COLLIER ON BANKRUPTCY}, supra note 10, \$ 1104.01, at 1104-21 (emphasis added). In the opinion of these authors, this is an incorrect interpretation of the statute. Section 1104(a)(1) clearly states that the court shall appoint a trustee for cause, "either before or after the commencement of the case." (emphasis added). \textit{See also In re} Anniston Food-Rite, Inc., 20 Bankr. 511, 515 (Bankr. N.D. Ala. 1982).


\textsuperscript{77} Dardarian v. La Sherene, Inc. (\textit{In re} La Sherene, Inc.), 3 Bankr. 169, 175 (Bankr. N.D. Ga. 1980). \textit{Accord In re} Covenant Living Centers, Inc., No. 81-02663 (Bankr. E.D. Wis. Nov. 12, 1981) (unpublished opinion). Bankruptcy Judge Norton's succinct analysis of section 1104(a)(1) in \textit{La Sherene} may provide the basis for a motion \textit{in limine} by the moving party. Arguably, it would be prudent litigation strategy to move to limit or otherwise strike any proffered testimony concerning "future plans, revealed by current management." \textit{La Sherene}, 3 Bankr. at 175.
The particular kinds of conduct that have been found to satisfy the "for cause" standard are not easily susceptible of classification. Nevertheless, there are a number of cases where the courts have appointed trustees based upon an adequate showing of: irreconcilable conflicts of interest;\(^7^8\) com-


It should be noted that the mere fact that a debtor corporation engages in business with its subsidiaries or with related corporations does not *de jure* establish a conflict of interest justifying the appointment of a trustee. *See In re* F.A. Potts & Co., Inc., 20 Bankr. 3, 4 (Bankr. E.D. Pa. 1981).

\(^7^9\) The "commingling" cases are obviously analytically akin to those cases cited in *supra* note 77, where the courts found that certain conflicts of interest justified the appointment of a trustee. A representative sampling of commingling cases includes *In re* Brown, 31 Bankr. 583, 585 (D.D.C. 1983) (commingling of affairs of the corporation and individuals, exemplified by use of corporate funds to finance individuals' litigation); *In re* Philadelphia Athletic Club, Inc., 20 Bankr. 328, 334 (E.D. Pa. 1982) (siphoning of funds from the debtor corporation for personal use by the owner); *In re* Casco Bay Lines, Inc., 17 Bankr. 946, 949 (Bankr. 1st Cir. 1982) (appropriation and wrongful use of corporate assets for individual benefit); *In re* Ford, 36 Bankr. 501, 504-05 (Bankr. W.D. Ky. 1983) (postpetition sale and commingling of estate assets without court approval); *In re* Visch schoonmaker, Ossendryver Galleries Int'l, Inc., 35 Bankr. 816, 820 (Bankr. D. Hawaii 1983) (substantial intermingling without ade-
mingling of assets;\textsuperscript{79} inadequate accounting records or controls;\textsuperscript{80} failure to pay taxes,\textsuperscript{81} especially employee with-

\begin{quote}


The failure to maintain adequate accounting controls is also indirectly evidenced in cases where the debtor failed to obtain proper insurance, either for its employees or for its property and goods. \textit{See, e.g.,} American Metal Corp. v. Cowley (\textit{In re Cowley}), No. 82-20972 (Bankr. D. Kan. Dec. 1, 1983) (after-hours theft of property); \textit{In re} Caroline Desert Disco Inc., 5 Bankr. 536, 537 (Bankr. C.D. Cal. 1980) (insufficiency of maintenance and security at the debtor's premises).

Similarly, the bankruptcy courts have shown no tolerance for the mismanaging debtor in possession who fails to obtain proper insurance, either for its employees or for its property and goods. \textit{See, e.g.,} \textit{In re} Brown, 31 Bankr. 583, 585 (D.D.C. 1983) (failure to obtain proper insurance for both employees and property); \textit{Caroline Desert Disco, Inc.}, 5 Bankr. at 537 (failure to maintain necessary casualty, public liability and worker's compensation insurance).

\end{quote}
holding taxes; dishonesty; and fraud. The courts have also ordered the appointment of a trustee where the debtor in possession has consistently violated the applicable local rules, and where the debtor in possession has either failed


to make payments to a secured party or has made unauthorized payments including, for example, payments on account of prepetition indebtedness.

Significantly, the courts have also recognized the importance of current management's ability to garner the confidence of major secured parties, unsecured creditors, and prospective buyers, and have shown little hesitancy to appoint a trustee in those instances in which the debtor in possession lacked credibility or failed to instill confidence, or where, by analogy, the debtor in possession displayed an inability to effectuate a plan of reorganization. Finally, the incompetence or gross mismanagement. See generally In re Modern Office Supply, Inc., 28 Bankr. 943, 944 (Bankr. W.D. Okla. 1983) (discussing the reporting duties of a debtor in possession); In re Sea Queen Kontaratos Lines, Ltd., 10 Bankr. 609, 610 (Bankr. D. Me. 1981) (suggesting, in dictum, that a local rule violation is per se gross mismanagement). But cf. In re Crescent Beach Inn, Inc., 22 Bankr. 155, 160 (Bankr. D. Me. 1982) (despite evidence of Local Rule 2007(b)(2) violation, no appointment; contrary to Sea Queen Kontaratos Lines, court expressly declines to adopt a per se rule).

86. See, e.g., In re McCall, 34 Bankr. 68, 69 (Bankr. E.D. Pa. 1983) (debtor's failure to make any monthly payments to mortgagees over a two-year period constituted gross mismanagement or incompetence); In re JP Enter., Inc., 22 Bankr. 661, 662 (Bankr. E.D. Pa. 1982) (debtor's failure to make any rental payments to landlord over a long period of time constituted gross mismanagement).

87. See, e.g., In re Ford, 36 Bankr. 501, 504 (Bankr. W.D. Ky. 1983) (failure to obtain court approval for postpetition transfer of assets); In re Bonded Mailings, Inc., 20 Bankr. 781, 784 (Bankr. E.D.N.Y. 1982) (debtor had been creating and repaying alleged loans without the benefit of court authorization or sufficient documentation).

88. See, e.g., In re Eastern Consol. Utils., Inc., 3 Bankr. 591, 592 n.3 (Bankr. E.D. Pa. 1980) (debtor had paid money on account of prepetition debts after the filing of the petition).


90. See, e.g., In re McCall, 34 Bankr. 68, 70 (Bankr. E.D. Pa. 1983) (trustee necessary to manage and sell property); In re Brown, 31 Bankr. 583, 583-84 (D.D.C. 1983) (chronic failure to develop property); In re Horn & Hardart Baking Co., 22
courts have appointed a trustee to investigate and report to
the court on the issue of whether the case should be con-
verted,\textsuperscript{91} and in those instances where the debtor was either
thrown out of possession\textsuperscript{92} or where an individual Chapter
11 debtor died.\textsuperscript{93}

\textbf{B. Appointment of a Trustee Under the "Best
Interests" Standard}

The authors of the leading bankruptcy treatise, \textit{Collier on
Bankruptcy}, have astutely observed that "there are few situ-
ations which come to mind where grounds will exist for the
appointment of a trustee under subsection (a)(2) where
'cause' for such appointment will not [also] exist under sub-
section (a)(1)."\textsuperscript{94} Nevertheless, there are a number of in-
stances in which the courts have appointed a trustee under
the "best interests" standard. Not surprisingly, however, the
case law tends to support \textit{Collier}'s analysis. It is not uncom-
mon to find decisions appointing a trustee resting upon both
the "for cause" and the "best interests" standards.

The particular kinds of conduct that have been found to
have satisfied the "best interests" standard are equally im-
mune to simple categorization, particularly since the "best
interests" standard necessarily requires the court to carefully
weigh competing equities.\textsuperscript{95} Nevertheless, the courts have
appointed trustees where the debtor in possession main-

\textsuperscript{91} For examples of cases in which a trustee appointed to investigate debtor's
financial history and report to the court on the issue of whether the case should be
converted to Chapter 7 see \textit{In re Steak Loft of Oakdale, Inc.}, 10 Bankr. 182, 186
(Bankr. E.D.N.Y. 1981) and \textit{In re Hotel Assoc., Inc.}, 7 Bankr. 130, 132 (Bankr. E.D.
Pa. 1980).

\textsuperscript{92} See, \textit{e.g.}, \textit{In re Casco Bay Lines, Inc.}, 17 Bankr. 946, 951-52 (Bankr. 1st Cir.
1982).

\textsuperscript{93} In support of the proposition that the death of an individual debtor in a non-
joint Chapter 11 case is sufficient cause for the appointment of a trustee, see \textit{In re

\textsuperscript{94} \textit{5 Collier on Bankruptcy, supra} note 10, ¶ 1104.01, at 1104-22 to -23.

\textsuperscript{95} \textit{See supra} text accompanying notes 61-65.
tained inadequate books and records, was involved in grave conflicts of interest, or was guilty of commingling assets of the corporation. The courts have also appointed a trustee under the "best interests" standard to investigate whether reorganization is possible, and, if so, to propose a plan of reorganization. Finally, like the cases under the "for cause" standard, the courts have appointed a trustee where the debtor in possession failed to maintain the confidence of the secured parties, and in some more unusual


97. See, e.g., In re Great N.E. Lumber & Millwork Corp., 20 Bankr. 610, 611-12 (Bankr. E.D. Pa. 1982) (best interests of creditors to have trustee appointed to investigate debtor's relationship to affiliated entities); In re Philadelphia Athletic Club, Inc., 15 Bankr. 60, 63 (Bankr. E.D. Pa. 1981) (trustee appointed to investigate admittedly adverse interests between operator of the debtor and the debtor's equity security holders); Smith v. Concord Coal Corp. (In re Concord Coal Corp.), 11 Bankr. 552, 554 (Bankr. S.D.W. Va. 1981) (substantial doubt as to whether current management was loyal to the goal of rehabilitation in view of current management's competing business interests and the potential for intercompany dealing); In re L.S. Good & Co., 8 Bankr. 312, 315 (Bankr. N.D.W. Va. 1980) (trustee necessary to investigate and evaluate grave potential conflicts of interest); Dardarian v. La Sherene, Inc. (In re La Sherene, Inc.), 3 Bankr. 169, 176 (Bankr. N.D. Ga. 1980) (internal officer disputes and management conflicts made it necessary to appoint trustee under section 1104(a)(2)).


100. See, e.g., In re L.S. Good & Co., 8 Bankr. 312, 315 (Bankr. N.D.W. Va. 1980) (appointment of trustee in "best interests" of parties because trustee's sole motivation will be to realize the maximum amount of monies possible); In re Vincent, 4 Bankr. 23, 25 (Bankr. M.D. Tenn. 1980) (where a trustee had been appointed, the debtor lost the exclusive right to file a plan in a Chapter 11 proceeding); Hotel Assocs., Inc. v. Trustees of Cent. States S.E. & S.W. Areas Pension Fund (In re Hotel Assocs., Inc.), 3 Bankr. 343, 345 (Bankr. E.D. Pa. 1980) ("There is need for the proposal of a plan by a person other than the debtor and such a need is a justification for the appointment of a trustee under § 1104(a)(2).") See generally King, supra note 10, at 115-16.

situations, such as where the debtor was confined in prison, or where the individual Chapter 11 debtor died following the filing of the petition. In analyzing the “best interests” standard, the courts have exhibited a natural reluctance to invoke their discretion to appoint a trustee in marginal cases. For example, the courts have declined to appoint a trustee where current management has a needed expertise in a complex industry, or where it was unclear whether a trustee was any more likely to successfully rehabilitate the debtor than the debtor in possession. Similarly, at least one court has declined to appoint a trustee where the sole purpose of the motion was to deprive the debtor in possession of its right to the 120 day exclusive period to file a plan. Finally, the courts have sometimes declined to appoint a trustee under the “best interests” standard where the intermediate option of appointing an examiner under section 1104(b) proved to be a more palatable option. However, it is safe to conclude

carry weight in section 1104(a)(2) analysis); In re Crescent Beach Inn, Inc., 22 Bankr. 155, 160 (Bankr. D. Me. 1982) (largest secured creditors willing to work with current management).


106. See, e.g., In re Tyler, 18 Bankr. 574, 578 (Bankr. S.D. Fla. 1982).


108. See, e.g., In re Hamiel & Sons, Inc., 20 Bankr. 830, 832-33 (Bankr. S.D. Ohio 1982) (in view of the costs of trustee and the fact that estate was not being depleted, the court would employ “intermediate procedure” of appointing an examiner to investigate the potential liabilities of principal officers and shareholders under alter ego doctrine); In re Burnside, Lee & Harris Diamond Co., 17 Bankr. 104, 106-07 (Bankr. M.D. Fla. 1981) (in view of the limited operation of debtor’s business, only necessary to appoint examiner); In re Liberal Mkt., Inc., 11 Bankr. 742, 744-45 (Bankr. S.D. Ohio 1981) (absent evidence of “cause” under section 1104(a)(1), “best interests” of all parties better served by appointing an examiner and vesting the exam-
that even the appointment of an examiner is an extraordinary remedy.\textsuperscript{109}

III. \textbf{THE ADVANTAGES OF A \textit{CHAPTER} 11 \textit{TRUSTEE}}

It is axiomatic that the appointment of a trustee has significant consequences,\textsuperscript{110} and that the decisions made by the trustee will have a critical impact on the outcome of the case.\textsuperscript{111} In a very real sense, the mere displacement of a fraudulent, dishonest, incompetent, or grossly mismanaging debtor in possession is the greatest advantage flowing from the appointment of a Chapter 11 trustee.\textsuperscript{112}

In the opinion of these authors, although there are indisputably certain drawbacks in seeking the appointment of a trustee,\textsuperscript{113} where warranted, the advantages far outweigh the...
disadvantages and make the motion to appoint a trustee a powerful tool for the protection of creditors’ rights. In the prosaic words of Bankruptcy Judge King in In re Hotel Associates, Inc.,115 “[t]he trustee will seek to benefit all the creditors and will bring a refreshing air of objectivity and impartiality to a business . . . .”116 More specifically, the trustee will hopefully keep accurate and trustworthy records,

expenses of the additional layer of professional persons retained by the trustee, may outweigh any benefits gained, or even preclude the successful reorganization of the business; (2) the appointment of a trustee ousts the debtor, who is more familiar with the business, and whose leadership may be necessary during the reorganization; (3) the trustee will necessarily have to take time to familiarize himself or herself with the business, which may prove detrimental to the chances for successful rehabilitation; and (4) the too-frequent appointment of trustees may discourage debtors from seeking the benefit of Chapter 11 until it is too late. See HOUSE REPORT, supra note 2, at 232-34, reprinted in 1978 U.S. CODE CONG. & AD. NEWS at 6191-94. See also In re Bonded Mailings, Inc., 20 Bankr. 781, 785 (Bankr. E.D.N.Y. 1982) (“[T]he appointment of a trustee will generally necessitate the displacement of the current experienced management with those probably less familiar with the field at a time when the enterprise itself is usually tottering on the brink of financial collapse.”); supra note 104 and accompanying text. See generally Coogan, Broude & Glatt, supra note 10, at 1156; and Note, The Misbehaving Debtor, supra note 10, at 479.

Additionally, the appointment of a trustee may harm the prospects for reorganization in those instances where long-term customers or suppliers, understandably loyal to the debtor, may refuse to deal with a trustee or to extend credit to the trustee. This may, in turn, cause the secured creditors to be less cooperative because of the perceived loss of customers. Conversely, the trustee himself may be inadequate, or may be too quick to seek a liquidation rather than a time-consuming rehabilitation of the business. Even worse, the trustee’s mere presence may mistakenly signal liquidation to the creditors.

A trustee may also prove to be the wrong solution where the appointment engenders fear and distrust among the employees, particularly those loyal to former management. Similarly, the appointment may cause an acute lack of cooperation from the debtor’s management or counsel.

Finally, a Chapter 11 trustee may be totally unnecessary where the appointment of an examiner or conversion to Chapter 7 would better serve the interests of the creditors, equity security holders, and all others.

116. Id. at 346. See also Dardarian v. La Sherene, Inc. (In re La Sherene, Inc.), 3 Bankr. 169, 176 (Bankr. N.D. Ga. 1980), where Bankruptcy Judge Norton, perhaps a sailor himself, eloquently observed that a trustee will provide “a fiduciary protective shield,” and that:

The estate obviously needs a properly experienced, firm, clear-headed, far-sighted helmsman to chart an altered, cautious and steady course, with full command of the bridge, power, rudder, manifest, cargo and crew, if the cross-winds and heavy seas of adversity presently confronting this business enterprise are to be successfully traversed.
attempt to cooperate with creditors in the pursuit of a plan, and provide invaluable intangible support for the reorganization potentiality of the debtor. Moreover, the trustee's objective management of the business may make it possible to sever uneconomical loyalties to favored suppliers, customers or employees, sell off or abandon unprofitable or marginal divisions or product lines, reduce overhead by cutting out inefficiencies, waste and excesses, and otherwise instill the confidence of the creditors, equity security holders, and the bankruptcy judge who appointed the trustee.

This same objectivity will enable the trustee to make a realistic decision on the issue of whether the business should be continued, sold or liquidated. In many instances, the presence of a disinterested trustee may be critical in ameliorating the differences between a major creditor and the debtor. At a minimum, a trustee will have collected the requisite information to propose and confirm a plan over the objection of a recalcitrant creditor.

Moreover, because the trustee will be free of any untoward conflicts of interest, he or she will be able to investigate insider transactions, commence avoidance or preference actions, particularly where the debtor refuses to answer any questions on the basis of a claim of privilege, and investigate the relationship between the debtor and pre-bankruptcy or postbankruptcy counsel.

117. LoPucki, supra note 10, at 257.
118. See supra text and accompanying notes 91 & 99-100.
120. See, e.g., id.
121. See supra text and accompanying notes 78-79, & 97-98.
122. See id.
124. See, e.g., Dardarian v. La Sherene, Inc. (In re La Sherene, Inc.), 3 Bankr. 169, 176 (Bankr. N.D. Ga. 1980). In this regard, the appointment of a trustee may produce an additional, indirect benefit in delimiting or wholly eliminating the role of the debtor's chosen bankruptcy counsel, particularly where one cause of the debtor's difficulties leading to the appointment of a trustee resulted from ill-advised legal counsel. See also In re Eastern Consol. Utils., Inc., 3 Bankr. 591, 593 (Bankr. E.D. Pa. 1980). Moreover, once a trustee is appointed, he or she is entitled to seek permission to retain counsel, and this counsel is likely to supplant the debtor's counsel, if for no other reason, because it is well established that "[t]he debtor's attorney may not be compensated for services which duplicate those of the trustee or the attorney for the
In some instances, the appointment of a trustee may also prove to be particularly advantageous where the court has an opportunity to appoint an individual or firm with expertise. 2 COLLIER ON BANKRUPTCY ¶ 327.07, at 327-33 (15th ed. 1982). See also In re Designaire Modular Home Corp., 517 F.2d 1015, 1019 (3d Cir. 1975); In re Eureka Upholstering Co., 48 F.2d 95 (2d Cir. 1931); In re Pajari Am. Indian Art, Inc., 11 Bankr. 807, 811 (Bankr. D. Ariz. 1981).

The diminished role of debtor's counsel is also attributable to the operation of the Bankruptcy Code itself. As noted above, the interplay of sections 1107 and 1108 creates the logical inference that, once a trustee is appointed, the debtor is divested of any power to control the debtor corporation. See 11 U.S.C. §§ 1107-1108 (1982). See also In re O.P.M. Leasing Servs., Inc., 13 Bankr. 54, 58 (Bankr. S.D.N.Y. 1981) ("as far as a reorganizing debtor is concerned, the trustee possesses and controls its assets, conducts its affairs, and subordinates management, if any, serves at the trustee's pleasure"), aff'd, 670 F.2d 383 (2d Cir. 1982). Accordingly, although the debtor and its counsel have the right to be heard, the debtor's counsel may only be compensated for those services which actually benefit the estate and do not duplicate the services rendered by the trustee's attorney. See also In re Pajari Am. Indian Art, Inc., 11 Bankr. 807 (Bankr. D. Ariz. 1981); 2 COLLIER ON BANKRUPTCY, ¶¶ 330.04[3], 330.05[2][d]; Butenas, Establishing Attorney's Fees Under the New Bankruptcy Code, 87 COMM. L.J. 237 (1982); Herzog, Fees and Allowances in Bankruptcy, 36 CONN. B.J. 374, 381 (1962). See generally Randolph & Randolph v. Scruggs, 190 U.S. 533 (1903); In re Hamilton Hardware Co., 11 Bankr. 326, 329-30 (Bankr. E.D. Mich. 1981); In re Garland Corp., 8 Bankr. 826, 830 (Bankr. D. Mass. 1981); In re G.W.C. Fin. & Ins. Servs., Inc., 8 Bankr. 122, 124 (Bankr. C.D. Cal. 1981); In re Sumthin' Special, Inc., 2 Bankr. 743, 748 (Bankr. N.D. Ill. 1980) (the debtor's attorney "clearly cannot be compensated for unnecessary work which did not benefit the estate").

Finally, although the scope of this article does not permit an in-depth analysis of the ramifications incident to the diminished role of debtor's counsel, it would not be surprising to find the trustee objecting to the award of any administrative expenses to the debtor's counsel for fees incurred in resisting the appointment of a trustee, particularly when the bankruptcy court ultimately appoints a trustee "for cause." For example, the trustee could argue that the debtor's resistance not only produced no benefit to the estate, but "in fact obstructed and impeded the administration of the case . . . ." In re J.V. Knitting Service, Inc., 22 Bankr. 543, 545 (Bankr. S.D. Fla. 1982). See also In re Laister-Kaufmann Aircraft Corp., 101 F. Supp. 950, 955-56 (E.D. Mo. 1952) (court denied fees incurred by debtor in opposing and delaying settlement with government). Moreover, to the extent that the debtor's counsel's defense of current management was actually a defense of an individual officer or director, an award of fees may be inappropriate since the time spent inured only to the personal benefit of these individuals, not the estate. See, e.g., In re Rosen, 25 Bankr. 81, 86 (Bankr. D.S.C. 1982). Finally, to the extent that the debtor's defense to the motion for the appointment of a trustee is frivolous or without merit, no award of fees should be forthcoming. See In re Underground Utils. Constr. Co., Inc., 13 Bankr. 735, 738 (Bankr. S.D. Fla. 1981). Cf. In re Garland Corp., 8 Bankr. 826, 837 (Bankr. D. Mass. 1981) (ethical duty to defend client's interest so long as the actions are not frivolous or devoid of substance); BANKR. R.P. 19011.

125. The appointment of a trustee is governed by sections 1104(c) or 151104(c) depending upon whether the particular judicial district is a pilot district. 11 U.S.C.
unique expertise,\textsuperscript{126} or to counterbalance an otherwise ineffective creditors' committee.\textsuperscript{127} Finally, and perhaps most importantly, the trustee may be more experienced than debtor management in dealing with the tangle of the reorganization process, thereby maximizing the chances of a successful reorganization for the benefit of all parties to the proceeding. In a word, the trustee is likely to be free of the prejudices and strife within the debtor's business hierarchy, and therefore more open to creative solutions.

\textsuperscript{126} See supra note 70 for a discussion of the appointment process in a pilot district.

Pursuant to sections 1104(c) and 151104(c) the court may appoint a "disinterested person" as a trustee. Section 101(13) defines the term "disinterested person" and section 321 governs who is eligible to serve as a trustee. The deliberate use of the word "person" in these sections, particularly in view of the related definition of the word "person" in section 101(30), makes it clear that the trustee need not be an individual, but could also be a corporation. This option may provide the court with greater flexibility. For example, in the reorganization of a large real estate entity, the court may wish to appoint a real estate management firm as trustee. Moreover, the absence of any residency requirement allows the court to utilize the unique services of individuals or corporations outside the immediate judicial district. See 11 U.S.C. § 321(a)(1) (1982). In any event, the court may not appoint a partnership or governmental unit to act as trustee, nor the United States Trustee, the examiner, or a relative of any judge of the court. 11 U.S.C. §§ 101(30), 321, 151104(c) (1982); BANKR. R.P. 5002.

Because there is no requirement that the court appoint a trustee from the panel of private trustees, the prevailing party may wish to interview and submit a list of prospective candidates to the court. In this way, the court will have a greater opportunity to match a prospective trustee's abilities with the needs of the case. See also BANKR. R.P. 2008-2010, 2012-2013 regarding the notification and acceptance of appointment; posting and acceptance of the trustee's bond; appointment of trustees in jointly administered cases; death, resignation or removal of trustees; and annual aggregate compensation of individual trustees. The appropriate amount of the trustee's bond and the sufficiency of the surety of such a bond is determined by the court under section 322(b).

\textsuperscript{126} For example, in \textit{In re} Covenant Living Centers, Inc., No. 81-02663 (Bankr. E.D. Wis. Nov. 12, 1981) (unpublished opinion), the bankruptcy court appointed a trustee with unique and invaluable expertise in the management and rehabilitation of failing lifetime care retirement centers.

\textsuperscript{127} See also LoPucki, supra note 10, at 249. Conversely, the courts have held that creditors' committees have a right to commence adversary proceedings, or intervene in existing proceedings, where the trustee has been lax or ineffectual. See generally Blain & Erne, \textit{Creditors' Committees Under Chapter 11 of the United States Bankruptcy Code: Creation, Composition, Powers and Duties}, 67 MARQ. L. REV. 491 (1984) and cases cited therein.
IV. Conclusion

Although the congressional intent embodied in section 1104(a) and the case law emerging under that section places a heavy burden on the party seeking to displace debtor management, where justified, the appointment of a trustee may immeasurably enhance and facilitate the reorganization process. The right to have a trustee appointed, whether for cause or for the best interests of creditors, equity security holders and other interests of the estate, serves as an important counterweight to the debtor's otherwise broad right to remain in possession at the expense of the creditors and equity security holders. A motion for the appointment of a trustee is an important remedy that cannot be overlooked, and which may very well serve as the focal point for a successful reorganization.