

US Law Week

Justices Lob Bankruptcy Fee ‘Blank Slate’ Over to Lower Courts

By Alex Wolf

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- Justices say fee structure unconstitutional without mandating remedy
- Some appeals courts have said invalid fees must be refunded
- [Practical Guidance: US Trustee](#) (Bloomberg Law subscription)

Federal courts and debtors have been left to grapple with the impact of a US Supreme Court ruling that the structuring of fees bankrupt debtors pay to the US Trustee was unconstitutional.

Congress enacted a hike in Chapter 11 fees beginning in 2018 to address a budgetary shortfall for the US Trustee, the Justice Department’s bankruptcy watchdog. But because the increase didn’t affect debtors in the states of Alabama and North Carolina—where the US Trustee doesn’t operate—the hike violated a constitutional provision requiring uniform federal bankruptcy laws, the high court said June 6 in *Siegel v. Fitzgerald*.

The Supreme Court remanded the case to the U.S. Court of Appeals for the Fourth Circuit to sort out, rather than coming up with a solution for the debtor seeking a refund in the case.

In dodging the “thorny issue” of what to do next, the Supreme Court left open a large question not just for Circuit City trustee Alfred Siegel, but for Chapter 11 debtors across the country that have paid increased quarterly fees over the past few years, bankruptcy attorney Justin Paget of Hunton Andrews Kurth LLP said.

“What’s going to happen to those debtors in the 48 states that actually paid the fee increases?” Paget said. “It’s a significant administrative hurdle in my view to go and reverse the fees if they were actually paid.”

The US Trustee has estimated that approximately \$324 million worth of quarterly fees had been imposed on debtors after Congress raised the fees.

The big issue is now whether courts will force the government to give back “massive refunds,” said Cozen O’Connor attorney Robert M. Fishman.

“We’re operating on a blank slate,” Fishman said. “There’s just no telling what they might do.”

The Justice Department declined to comment.

Dual System

The Bankruptcy Judgeship Act of 2017 was intended to replenish the US Trustee's dwindling finances, enabling the Justice Department to continue its job of ensuring parties in bankruptcy cases don't operate outside the law. Fees were raised from a maximum of \$30,000 to a maximum of \$250,000, depending on how much the debtors' estate paid in disbursements that quarter.

Bankruptcy cases in Alabama and North Carolina are monitored by a bankruptcy administrator instead of a US Trustee. The roles are nearly identical, but the bankruptcy administrator system is overseen by the Judicial Conference of the United States instead of the Justice Department and its operations are funded through the judiciary's budget instead of debtor-paid fees.

Because the fee hike didn't affect bankruptcy administrator districts, companies like Circuit City began to argue that they were being forced to pay more for government services than similarly situated debtors in North Carolina and Alabama.

"There may have been some small effect for smaller cases but the fees only get substantial when the disbursements are pretty high," said University of Kentucky law professor Christopher Bradley.

Fee Refunds

As noted by the Supreme Court, the parties in Circuit City's case have disputed the appropriate remedy. While Siegel has asked for a full refund of fees paid during the "nonuniform period," the US Trustee has said relief should only be provided prospectively or debtors in the bankruptcy administrator districts should be forced to pay more.

"It looks like there are all these different options," said Bradley.

Other federal appeals courts have issued decisions suggesting how to treat debtors that have been charged the enhanced fees. Both the Second Circuit and the Tenth Circuit last year found that the lack of uniformity violated the Constitution, and determined fees must be refunded.

A proposed class of Chapter 11 debtors seeking a full refund of enhanced fees paid to the US Trustee beginning in 2018 is currently trying to figure out just how much the government should be giving back.

Proposed class counsel Bradley L. Drell of Gold Weems Bruser Sues & Rundell APLC said he believes the Fourth Circuit will have to award Circuit City a full refund or else "come up with a persuasive argument of why the Second and Tenth Circuits are wrong."

The issue could be further clarified as early as next week when the Supreme Court is expected to issue an order on whether it will hear the Justice Department's appeal from the Tenth Circuit's decision in the bankruptcy case for John Q. Hammons Hotels & Resorts, Drell said.

If the justices decline to take up the Hammons case, Drell believes it should boost his chances of certifying a class of claimants seeking a refund against the government. And even if the courts never reach a final remedy, he believes his case could at least provide a vehicle to settle the broad group of claims.

The Supreme Court decision, in which the justices stopped short of ruling on the constitutionality of having two different systems, also opens the door for a look at the dual structure itself, Drell said.

“In light of this, it wouldn’t surprise me if Congress decided to finally take this up and fix it,” Drell said.

To contact the reporter on this story: Alex Wolf in New York at awolf@bloomberglaw.com

To contact the editors responsible for this story: Keith Perine at kperine@bloomberglaw.com; Roger Yu at ryu@bloomberglaw.com

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