

APPENDIX C.

**PROPOSED AMENDMENTS TO
BANKRUPTCY RULES 5002 AND 5004**

PRELIMINARY DRAFT OF PROPOSED
AMENDMENTS
To
BANKRUPTCY RULES 5002 AND 5004

Public hearings will be held
on January 17, 1985 in
Washington, D. C.

COMMITTEE ON RULES OF PRACTICE
AND PROCEDURE
OF THE
JUDICIAL CONFERENCE OF THE
UNITED STATES

AUGUST 1984

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AND PROCEDURE

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COMMITTEE ON RULES OF PRACTICE AND PROCEDURE
OF THE
JUDICIAL CONFERENCE OF THE UNITED STATES
ADMINISTRATIVE OFFICE OF THE
UNITED STATES COURTS
WASHINGTON, D.C. 20544

TO THE BENCH AND BAR:

The Judicial Conference Advisory Committee on Bankruptcy Rules has proposed amendments to Bankruptcy Rules 5002 and 5004 and has requested that the proposed amendments be circulated to the bench and bar and to the public generally for comment. Committee Notes, prepared by the Advisory Committee and accompanying the proposed amendments, explain their intent and purpose.

The Judicial Conference Standing Committee on Rules of Practice and Procedure **has not yet approved these proposed amendments**, but submits them herewith for public comment. We request that all comments be placed in the hands of our Committee as soon as convenient and, in any event, no later than January 1, 1985.

All communications with respect to the proposed amendments to Bankruptcy Rules 5002 and 5004 should be addressed to the Committee on Rules of Practice and Procedure, Administrative Office of the United States Courts, Washington, D. C. 20544.

In order that persons and organizations wishing to do so may comment orally on these proposals, hearings on them will be held at the National Courts Building in Washington, D. C. on Thursday January 17, 1985. Those wishing to testify should contact the Secretary to the Committee at the above address prior to January 1, 1985.

These proposed amendments have not been submitted to nor considered by the Judicial Conference of the United States or the Supreme Court.

Edward T. Gignoux
*Chairman, Standing Committee on
Rules of Practice and Procedure*

Joseph F. Spaniol, Jr., *Secretary*

August 1, 1984
Washington, D. C.

PRELIMINARY DRAFT
OF PROPOSED AMENDMENTS TO
BANKRUPTCY RULES 5002 AND 5004*

Rule 5002. Prohibited Appointments.
Restrictions on Appointments

1 No person may be appointed as a trustee or examiner or
2 be employed as an attorney, accountant, appraiser,
3 auctioneer, or other professional person pursuant to § 327 or
4 § 403 of the Code if (1) the person is a relative of any judge
5 of the court making the appointment or approving the
6 employment or (2) the person is or has been so connected with
7 any judge of the court making the appointment or approving
8 the employment as to render such appointment or
9 employment improper. Whenever under this rule a person is
10 ineligible for appointment or employment, the person's firm,
11 partnership, corporation, or any other form of business
12 association or relationship, and all members, associates and
13 professional employees thereof are also ineligible for
14 appointment or employment.

*New matter is underscored; matter to be omitted is lined through.

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15 (a) Appointment of Relatives Prohibited. No
16 individual may be appointed as a trustee or examiner or be
17 employed as an attorney, accountant, appraiser, auctioneer,
18 or other professional person pursuant to § 327 or § 1103 of the
19 Code if the individual is a relative of the bankruptcy judge
20 making the appointment or approving the employment.
21 Whenever under this subdivision an individual is ineligible for
22 appointment or employment, the individual's firm,
23 partnership, corporation, or any other form of business
24 association or relationship, and all members, associates and
25 professional employees thereof are also ineligible for
26 appointment or employment.

27 (b) Judicial Determination that Appointment or
28 Employment Is Improper. A bankruptcy judge may not
29 appoint a person as a trustee or examiner or approve the
30 employment of a person as an attorney, accountant,
31 appraiser, auctioneer, or other professional person pursuant
32 to § 327 or § 1103 of the Code if that person is or has been so
33 connected with such judge as to render the appointment or
34 employment improper.

COMMITTEE NOTE

The amended rule is divided into two subdivisions. Subdivision (a) applies to relatives of bankruptcy judges and subdivision (b) applies to persons who are or have been connected with bankruptcy judges. Subdivision (a) permits no judicial discretion; subdivision (b) allows judicial discretion. In both subdivisions of the amended rule "bankruptcy judge" has been substituted for "judge." The amended rule makes clear that it only applies to relatives of, or persons connected with, the bankruptcy judge. See In re Hilltop Sand and Gravel, Inc., 35 B.R. 412 (N.D. Ohio 1983).

Subdivision (a). The original rule prohibited all bankruptcy judges in a district from appointing or approving the employment of (i) a relative of any bankruptcy judge serving in the district, (ii) the firm or business association of any ineligible relative and (iii) any member or professional employee of the firm or business association of an ineligible relative. In addition, the definition of relative, the third degree relationship under the common law, is quite broad. The restriction on the employment opportunities of relatives of bankruptcy judges was magnified by the fact that many law and accounting firms have practices and offices spanning the nation.

Relatives are not eligible for appointment or employment when the bankruptcy judge to whom they are related makes the appointment or approves the employment. Canon 3(b)(4) of the Code of Judicial Conduct, which provides that the judge "shall exercise his power of appointment only on the basis of merit, avoiding nepotism and favoritism," should guide a bankruptcy judge when a relative of a judge of the same bankruptcy court is considered for appointment or employment.

Subdivision (b), derived from clause (2) of the original rule, makes a person ineligible for appointment or employment if the person is so connected with a bankruptcy judge making the appointment or approving the employment as to render the appointment or approval of employment improper. The caption and text of the subdivision emphasize that application of the connection test is committed to the sound discretion of the bankruptcy judge who is to make the appointment or approve the employment. All relevant circumstances are to be taken into account by the court. The most important of those circumstances include: the nature and duration of the connection with the bankruptcy judge; whether the connection still exists, and, if not, when it was terminated; and the

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type of appointment or employment. These and other considerations must be carefully evaluated by the bankruptcy judge.

The policy underlying subdivision (b) is essentially the same as the policy embodied in the Code of Judicial Conduct. Canon 2 of the Code of Judicial Conduct instructs a judge to avoid impropriety and the appearance of impropriety, and Canon 3(b)(4) provides that the judge "should exercise his power of appointment only on the basis of merit, avoiding nepotism and favoritism." Subdivision (b) alerts the potential appointee or employee and party seeking approval of employment to consider the possible relevance or impact of subdivision (b) and indicates to them that appropriate disclosure must be made to the bankruptcy court before accepting appointment or employment. The information required may be made a part of the application for approval of employment. See Rule 2014(a).

Subdivision (b) departs from the former rule in an important respect: a firm or business association is not prohibited from appointment or employment merely because an individual member or employee of the firm or business association is ineligible under subdivision (b).

The emphasis given to the bankruptcy court's judicial discretion in applying subdivision (b) and the absence of a per se extension of ineligibility to the firm or business association or any ineligible individual complement the amendments to subdivision (a). The change is intended to moderate the prior limitation on the employment opportunities of attorneys, accountants and other professional persons who are or who have been connected in some way with the bankruptcy judge. For example, in all but the most unusual situations service as a law clerk to a bankruptcy judge is not the type of connection which alone precludes appointment or employment. Even if a bankruptcy judge determines that it is improper to appoint or approve the employment of a former law clerk in the period immediately after completion of the former law clerk's service with the judge, the firm which employs the former law clerk will, absent other circumstances, be eligible for employment. In each instance all the facts must be considered by the bankruptcy judge.

Subdivision (b) applies to persons connected with a bankruptcy judge. "Person" is defined in § 101 of the Bankruptcy Code to include an "individual, partnership and corporation." A partnership or corporation may be appointed or employed to serve in a bankruptcy case. If a bankruptcy judge is connected in some way with a partnership or corporation, it is necessary for the court to determine

whether the appointment or employment of that partnership or corporation is proper.

The amended rule does not regulate professional relationships which do not require approval of a bankruptcy judge. Disqualification of the bankruptcy judge pursuant to 28 U.S.C. § 455 may, however, be appropriate. Under Rule 5004(a), a bankruptcy judge may find that disqualification from only some aspect of the case, rather than the entire case, is necessary. A situation may also arise in which the disqualifying circumstance only comes to light after services have been performed. Rule 5004(b) provides that if compensation from the estate is sought for these services, the bankruptcy judge is disqualified from awarding compensation.

Rule 5004. Disqualification

1 (a) Disqualification of Judge. When a judge is
2 disqualified from acting by 28 U.S.C. § 455, he shall
3 disqualify himself from presiding over the adversary
4 proceeding or contested matter in which the disqualifying
5 circumstance arises or, if appropriate, he shall disqualify
6 himself from presiding over the case.

7 (b) Disqualification of Judge from Allowing
8 Compensation. A judge shall disqualify himself from allowing
9 compensation to a person who is a relative or with whom he is
10 so ~~associated~~ connected as to render it improper for him to
11 authorize such compensation.

COMMITTEE NOTE

The word "associated" in subdivision (b) has been changed to "connected" in order to conform with Rule 5002(b).