It is fundamental that the client gets to pick its lawyer. However, when representing estate fiduciaries, such as a debtor-in-possession ("DIP"), a trustee, or an official committee, counsel's hiring must be approved by the bankruptcy court. Parties-in-interest can object to a proposed counsel's retention for valid concerns about actual and potential conflicts of interest. Sometimes these objections, though, do not appear to be related to concerns about conflicts but are asserted for other purposes, such as to obtain a perceived litigation advantage. One common objection raised to an application to employ is that the proposed attorneys have not made full disclosure under Fed. R. Bankr. P. 2014(a) ("Rule 2014") of all "connections" they have to parties-in-interest in a bankruptcy case.

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Even in today's electronic age of Facebook and Twitter, many industries still rely on paper records to provide services, especially health care. Due to recent initiatives by the federal government, including the passage of the Health Information Technology for Economical and Clinical Health ("HITECH") Act as part of the American Recovery and Reinvestment Act ("ARRA"), hospitals and other health care providers are converting from paper to electronic medical records ("EMR"). EMR technology, however, has put a spotlight on the uncertainty with respect to the legal status of patient medical records, particularly after a hospital files bankruptcy.

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Please see the ABA Business Bankruptcy Committee web page, "Legislative News," for the most recent Legislative Update and other postings of recently proposed and enacted legislation prepared by the Legislation Subcommittee on the ABA Business Bankruptcy Committee.

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2011 Kathryn R. Heidt Memorial Award Presented to Corali ("Cori") Lopez-Castro

On October 13, 2011, the ABA Section of the Business Law Business Bankruptcy Committee was delighted to award the annual Kathryn R. Heidt Memorial Award to Miami attorney Corali ("Cori") Lopez-Castro.

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Watch Business Bankruptcy Webinars

In September 2011, the Business Bankruptcy Committee presented a webinar entitled, “Stern v. Marshall: Bombshell or a Dud.” The Committee also recently presented a webinar entitled, “DBSD: Does it Portend the End of Gifting to Junior Classes and Claims Purchasing?” Below is a link to the full webinars and to the slide show presentations.

» Business Bankruptcy Committee Webinars

Materials from the Business Bankruptcy Section 2011 Fall Meeting

At the Fall Meeting of the ABA Section of Business Law Business Bankruptcy Committee in Tampa Bay, members of the Committee presented a number of informative and interesting programs. Below is a link to all of the materials provided at these programs. (Access to some of the articles requires your ABA password.)

» 2011 Business Bankruptcy Fall Meeting Materials

Submit Articles for the Business Bankruptcy Newsletter

The Business Bankruptcy Committee invites you to submit articles for possible publication in future issues. The articles do not need to be long or in-depth, and it is a great way to get involved in the Business Bankruptcy Committee. Articles can survey the law nationally or locally, discuss particular business bankruptcy issues, or examine a specific case. If you are interested in submitting an article, please contact Newsletter Editor-in-Chief Christopher Alston at ALSTC@foster.com or Editor Marvin Ruth at MRUTH@lrlaw.com.
The “Connections” Conundrum: 
Compliance with Rule 2014 and a Call for Clarity and Guidance

by Jeffrey M. Sklarz and Sarah E. Pugh

It is fundamental that the client gets to pick its lawyer. However, when representing estate fiduciaries, such as a debtor-in-possession (“DIP”), a trustee, or an official committee, counsel’s hiring must be approved by the bankruptcy court. Parties-in-interest can object to a proposed counsel’s retention for valid concerns about actual and potential conflicts of interest. Sometimes these objections, though, do not appear to be related to concerns about conflicts but are asserted for other purposes, such as to obtain a perceived litigation advantage. One common objection raised to an application to employ is that the proposed attorneys have not made full disclosure under Fed. R. Bankr. P. 2014(a) (“Rule 2014”) of all “connections” they have to parties-in-interest in a bankruptcy case. The case law is uniform that even minor technical violations of Rule 2014’s disclosure requirements are sanctionable and the court has broad discretion to impose penalties for non-compliance.

Obviously, many of the concerns raised in such objections are valid, such as when counsel fails to disclose actual conflicts of interest that would/should be disqualifying, whether or not the case was subject to Rule 2014. On the other hand, the accidental failure to disclose immaterial “connections” should not constitute a valid basis for parties-in-interest to attempt to

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2 Sarah E. Pugh is a director at NHB Advisors, Inc., a national turnaround firm with "Proven Expertise in Corporate Renewal". Sarah's primarily focuses on financial advisory work for creditors' committees and debtors as well as liquidating trust services.
obtain a perceived advantage by filing a motion to disqualify counsel. However, there is no current safe harbor procedure in the form of a rule or U.S. Trustee’s guideline that, if followed, ensures compliance with Rule 2014. As explained below, recent case law continues to demonstrate that lawyers representing estate fiduciaries remain at risk for sanction, including disqualification and disgorgement of fees, for failing to disclose all “connections.” Accordingly, be it by an amendment to Rule 2014, local rule, U.S. Trustee guideline or otherwise, policies should be adopted so that counsel understands how to properly comply with and avoid the sometimes draconian consequences of not complying with Rule 2014.

**Retention Requirements for DIP and Committee Counsel**

Sections 327(a)\(^3\) and 1103(b) require that professionals retained by the DIP or a committee be “disinterested” and have no “adverse interest” to their client. Section 327(c) states the previous representation of a creditor of the debtor does not disqualify a professional from representing the DIP unless a party-in-interest objects to the retention and there is an actual conflict of interest.

Rule 2014(a) implements sections 327(a) and 1103(b) by requiring the “person to be employed” to identify “the person’s connections with the debtor, creditors, any other party in interest, their respective attorneys and accountants, the United States trustee, or any person employed in the office of the United States trustee.” The term “connections” is not defined either in the Rules or the Code. However, a common meaning is “a set of persons associated together.”\(^4\) Thus, nearly any relationship, regardless of how insignificant, could be argued to

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\(^3\) 11 U.S.C. § 327(a) speaks of the “trustee” retaining professionals. Under Chapter 11, a “debtor in possession” generally has the same powers and duties as a trustee. 11 U.S.C. § 1107.

constitute a connection. Despite the vague nature of the term “connection,” the degree of importance placed on disclosing all connections is quite high:

The disclosure requirements of Rule 2014 are strictly applied and impose an independent duty upon the professional applicant; thus, failure to comply with the disclosure rules is a sanctionable violation, even if proper disclosure would have shown that the professional had not actually violated any Bankruptcy Code provision or any Bankruptcy Rule.


Accordingly, even a benign and immaterial omission can lead to sanction.

**Case Law Interpreting Rule 2014(a)**

Unfortunately, cases interpreting Rule 2014(a) are not much help. Most cases do not make any effort to parse the meaning of “connection.” Rather, and quite understandably, a decision on whether to sanction or disqualify counsel for a Rule 2014 omission is very fact specific. The recent case of **Geisenberger v. DeAngelis**, 2011 U.S. Dist. Lexis 108916 (M.D. Pa. Sept. 23, 2011), presents a paradigm of the type of Rule 2014 omissions that will almost certainly lead to disqualification. There, debtor’s counsel failed to disclose “his extensive pre-petition connections” including representing creditors in pending litigation against the debtor and involvement in stock offerings of the debtor. Accordingly, ordering disqualification and disgorgement, the district court, affirming the bankruptcy court, held: “As a key participant in many of the Debtor’s pre-bankruptcy decisions – particularly the issuance of the stock certificates [to the creditor debtor’s counsel represented in litigation] – Geisenberger could not provide Debtor with a candid, disinterested evaluation of all possible options.” Id. at *23. See also, **In re Gluth Construction, Inc.**, 2011 Bankr. Lexis 4000 (N.D. Ill. Oct. 19, 2011) (counsel must disclose prior representations of debtor’s equity holders and fee guarantees).
While competent counsel should understand that actual conflicts and prior representation of creditors or equity holders of the debtor must be disclosed and may prohibit representing certain clients, there are many grey areas. In *Waldron v. Adams & Reese, LLCP (In re American International Refinery, Inc.)*, 436 B.R. 364 (W.D. La. 2010), debtor’s counsel was sanctioned for violating Rule 2014 for what appeared to be performing good work. A liquidation trustee appointed pursuant to the debtor’s confirmed plan brought an adversary proceeding against Adams & Reese, debtor’s chapter 11 counsel, seeking disgorgement of fees, including the prepetition retainer funded by the secured creditor: “[a]ccording to the Trustee, Adams & Reese had an incentive to favor GCA’s [the secured creditor] interests because of [the funding of the retainer] payment.” 436 B.R. at 373. Adams’s & Reese did not “fully disclose” the source of the prepetition retainer, certain terms of the lock-up agreement and Adams & Reese’s role as a pre-petition escrow agent. Id. at 379.

Despite specifically finding that Adams & Reese’s failure to disclose “does not reflect any prejudice or harm to estate or to its creditors,” and that the confirmed plan resulted in full payment of creditors and distributions to equity, the court sanctioned Adams & Reese by ordering disgorgement of 20% of its fees, concluding “[t]he disclosure lapses at issue here are significant because they implicate two of the central disputes in the bankruptcy case.” Id. at 380. The lesson to be taken from this case is that even quality representation is no defense to a deficient Rule 2014 disclosure.

In *In re Universal Building Products*, 2010 Bankr. Lexis 3828 (Bankr. D. Del. Nov. 4, 2010), proposed counsel for a creditors’ committee were disqualified because they failed to disclose their “connection” to a proxy for foreign creditors. In *Universal Builders*, two firms contacted a translator, Dr. Liu, they had used in other cases involving Asian companies to
contact several Asian creditors in the Universal Builders case. Neither the firm, nor Dr. Liu, had any relationship with the creditors. Based on the communications, the creditors retained Dr. Liu (and an associate of the translator) as their proxy for the creditors’ committee organizational meeting and the firms were retained, at Dr. Liu’s recommendation, as counsel. Dr. Liu then resigned as proxy and the firms retained him as their translator. Neither firm disclosed the extent of their relationship with Dr. Liu or the above facts in their Rule 2014 statement. Disqualifying the firms, the court held they “should have fully disclosed at the outset their efforts in support of Dr. Liu’s attempt to obtain proxies from creditors to attend the Committee formation meeting… The failure to provide complete and accurate disclosure at the outset warrants denial of the Committee Retention Applications.” Id. at *37. Accordingly, how a firm becomes engaged by an estate fiduciary also presents a Rule 2014 disclosure issue.

Conclusion: The Need for a Safe Harbor for Complying with Rule 2014

Complying with Rule 2014 should not be a guessing game. Its purpose is to provide the court and parties-in-interest information to ensure that estate fiduciaries are represented by disinterested and competent counsel. Courts should not have to adjudicate the impact of a failure to disclose obscure “connections” that are immaterial to representing a client effectively or that no reasonable checking procedure would identify. Does it matter if counsel’s father owned a Chevy (in the GM bankruptcy) or the creditor’s committee’s counsel’s daughter purchased a computer from Circuit City? In a hospital case, should the fact that your children were born at the hospital be disclosed? Often, providing too much information is just as meaningless as providing too little. Further, the duty to disclose “all connections” may conflict with other laws or contractual obligations.
A review of the case law and language of Rule 2014 demonstrates the substantial need for the development of a safe harbor procedure that counsel representing estate fiduciaries can follow to ensure they are meeting their obligations under Rule 2014. This is particularly true in contentious cases where other parties-in-interest can use arguably irrelevant Rule 2014 omissions to disqualify competent counsel for strategic purposes. Counsel and courts need clear guidance on what practices, if followed, ensure compliance with Rule 2014 vagaries.

The 2014 Task Force

In order to proactively assist counsel, the Business Bankruptcy Committee of the American Bar Association, Business Law Section established a Rule 2014 Task Force (the “Task Force”). The Task Force created a survey to collect data concerning how law firms and other professionals meet their Rule 2014 disclosure obligations:

https://docs.google.com/spreadsheet/viewform?formkey=dHo0ckk4S1FLQ3dKUlgbjdaYUtQ

Please take a moment and complete this short survey. The information will be kept confidential and enable the Task Force to formulate possible solutions to the issue described above.
The Costs of Compliance with Section 351:
What Happens When You Can’t Afford To Store Patient Medical Records?

By Jean R. Robertson, Esq.¹

Even in today’s electronic age of Facebook and Twitter, many industries still rely on paper records to provide services, especially health care. Due to recent initiatives by the federal government, hospitals and other health care providers are converting from paper to electronic medical records (“EMR”).

An industry supporting EMR initiatives has boomed due to our government’s position that converting paper medical records to electronic records is an important goal. This commitment to EMR became clear with the passage of the Health Information Technology for Economical and Clinical Health (“HITECH”) Act as part of the American Recovery and Reinvestment Act (“ARRA”).² The HITECH Act was “incorporated into the ARRA to promote the adoption and meaningful use of health information technology,”³ and it directed the Secretary of Health and Human Services to award money to states to “facilitate and expand the electronic movement and use of health information”⁴ by providing billions of dollars over four years to health care providers to help update their EMR systems.

EMR technology put a spotlight on the uncertainty with respect to the legal status of patient medical records, particularly after a hospital files bankruptcy. Some states already have laws requiring health care facilities to maintain medical records for a defined period of time. In 2005, the Bankruptcy Code was amended to establish a procedure for the disposal of medical

¹ Jean R. Robertson is a Partner and Chair of the Business Restructuring and Insolvency Practice Group at Calfee, Halter & Griswold LLP.
² 42 U.S.C.A. §300jj, et seq.
³ 45 C.F.R. §160.
records when there is a bankruptcy and the debtor cannot afford to store them under state or federal law.

- **Storing and Destroying Patient Medical Records under Federal and State Law**

The Bankruptcy Abuse Prevention and Consumer Protection Act (“BAPCPA”) created Section 351, which governs the disposal of patient medical records by a debtor that is a “health care business.”

Although Section 351 is relatively new, there is a mature body of non-bankruptcy law dealing with the storage and disposal of medical records. Medicare and Medicaid, for example, generally require hospitals to retain a patient’s records for at least five (5) years. In New York, the law requires patient records be retained for at least six (6) years. Pursuant to Section 351 and Federal Rule of Bankruptcy Procedure 6011, when a health care debtor lacks funds to pay for medical record retention (paper and electronic) in accordance with applicable federal and state law, the debtor must take steps to safeguard such medical records.

Essentially, after 365 days, if medical records remain unclaimed, the trustee is required to send a written request to each appropriate federal agency requesting permission to deposit the records with such agency. Section 351 neither identifies the appropriate federal agencies, nor requires any agency to accept such records or impose any time limit by which a response must be received. If no federal agency accepts the records, the trustee may dispose of them by shredding, burning or otherwise permanently destroying the records so that they cannot be retrieved. The trustee must file a report with the court within 30 days certifying that the medical records have been destroyed, including an explanation of the method used to destroy them.

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7 N.Y. Comp. Codes R. & Regs. tit. 8, §29.2(a)(3).
- **Challenging and Addressing the Costs Imposed by Section 351**

  Even if the debtor’s prepetition lender does not have a blanket lien, it is likely that the debtor’s post-petition lender will be granted a security interest encumbering all assets. A debtor may be able to assert that the extent of the lender’s blanket post-petition lien is proof that it does not have sufficient funds to pay for records storage and retention. To avoid this position, parties who are active at the beginning of the case when a DIP or cash collateral order is entered (i.e., the U.S. Trustee or the committee) would need to insist that the post-petition financing include a carve-out to pay for future medical record storage.

  In addition, BAPCPA added Section 503(b)(8)(A), which provides that costs under Section 351 are entitled to administrative priority. If post-petition financing does not include a carve-out for this administrative expense, these costs may effectively reduce any recovery for unsecured creditors. Worst case, no carve-out means storage and disposal costs may need to be funded from the proceeds of avoidance actions that would otherwise be distributed to unsecured creditors.

  Also, a debtor may try to surcharge a lender’s collateral to pay medical record storage costs. Section 351’s legislative history suggests Congress intended such costs be surcharged against a secured creditor’s collateral if the debtor is administratively insolvent. However, Section 506(c) was not amended to provide for such a surcharge, nor was the general legal standard for awarding a surcharge changed so that it does not require a surcharge be limited to an amount equal to the extent of a benefit received by a secured party. In most circumstances, it could be very difficult to demonstrate that a secured party receives a benefit from the debtor’s ability to dispose of records.

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9 H.R. Rep. No. 109-31, pt. 1, at 139 (2005) (stating that “[i]t is anticipated that if the estate of the debtor lacks the funds to pay for the costs and expenses related to the disposal of patient records, the trustee may recover such costs and expenses under 11 U.S.C.A. 506”).
• **Conclusion**

In sum, the Bankruptcy Code and non-bankruptcy law require debtors in the health care business to preserve patient medical records for specified periods of time and to dispose of such records in specific ways. Compliance with these statutes imposes financial and administrative burdens on these estates. Health care debtors and their counsel should develop a strategy before filing to address these costs during the case so to maximize distributions to unsecured creditors.
On October 13, 2011, the ABA Section of the Business Law Business Bankruptcy Committee was delighted to award the annual Kathryn R. Heidt Memorial Award to Miami attorney Corali (“Cori”) Lopez-Castro. Kate died unexpectedly in May of 2005 at the age of 51. At the time of her death, she was the chair of the ABA Section of Business Law’s Business Bankruptcy Committee. This memorial award honors Kate’s memory. Kate was a tenured member of the faculty at the University of Pittsburgh School of Law. She was an accomplished author, scholar, teacher, lawyer, and administrator. In addition to her leadership roles at the ABA, she served in leadership capacities at the American Association of Law School’s Section on Creditors’ and Debtors’ Rights. She was a counselor in the truest sense of the word -- a wonderful mother, a friend to many, a dedicated mentor to students and young lawyers, and a trusted voice of wisdom who left us too soon. This Award is designed to serve as a lasting tribute to all she was and all for which she stood and to recognize the importance of bankruptcy education and scholarship to the ABA Business Bankruptcy Committee and the bankruptcy profession.

Mrs. Lopez-Castro stated that she is incredibly honored to have received the Award, and that “gratifying did not even capture” what it meant to have the Memorial Award Selection Committee speak so eloquently about Kate before presenting Mrs. Lopez-Castro with the award. Mrs. Lopez-Castro spent a lot of time with Kate, is deeply grateful for her tutelage, and most admired how “humble and effective” Kate was, taking to heart the lesson that “humility can be effective in a lawyer.”

Mrs. Lopez-Castro is a shareholder and the managing partner at Kozyak Tropin & Throckmorton. She concentrates her practice on bankruptcy and commercial litigation matters. Mrs. Lopez-Castro’s practice reflects her extensive experience and expertise in a wide range of bankruptcy and insolvency matters, including bankruptcy reorganizations and liquidations under the United States Bankruptcy Code, receiverships, workouts, debt restructuring, and creditors’ rights. Her practice also involves commercial litigation matters that arise from receiverships and liquidations. Serving on the panel of Trustees for the Southern District of Florida between 1998 and 2002, Mrs. Lopez-Castro was responsible for monetizing assets in bankruptcy cases filed in the United States Bankruptcy Court for the Southern District of Florida.

Mrs. Lopez-Castro is also the co-chair of the Pro Bono Sanding Committee of the Florida Bar and was the co-chair for the most recent fund raising campaign of Legal Services of Greater Miami, Inc., which provides free civil legal services to the neediest individuals in the Miami community. As a bankruptcy lawyer, Mrs. Lopez-Castro has seen first hand the effect the economy has had on her community, and her dedication to pro bono services reflects her deeply held conviction that the bankruptcy bar has an obligation to provide pro bono services and “show the community that we have a heart and a soul,” particularly in these difficult economic times.

In 2006 Mrs. Lopez-Castro was elected President of the Cuban American Bar Association, the largest voluntary bar association in Florida. Mrs. Lopez-Castro was the second woman president of the Cuban American Bar Association.

Ms. Lopez has earned Martindale-Hubbell’s highest rating (AV), and from 2005 through 2010 has been recognized in Chambers USA’s America’s Leading Lawyers for Business, an
independent, objective rankings guide to the nation’s top attorneys. In addition, Mrs. Lopez-Castro has been recognized repeatedly in *Florida Trend’s Legal Elite* for her practice in business law. The University of Miami Law Alumni Association awarded its first ever Leadership Award to Mrs. Lopez-Castro.

In addition to her involvement in the Cuban American Bar Association, Mrs. Lopez-Castro has lectured on bankruptcy-related topics at meetings and seminars of the American Bar Association (ABA), and is active in the ABA Business Bankruptcy Committee, other professional organizations, and the community.

Mrs. Lopez-Castro, who was born in San Juan, Puerto Rico, earned her J.D. degree, *cum laude*, in 1990 from the University of Miami School of Law, where she was a member of the *Inter-American Law Review*. She earned her Bachelor’s degree from Brown University in 1987.
Eligibility for the Award

In order to be eligible to receive the Kathryn R. Heidt Memorial Award, individuals must meet the following criteria:

• Be an attorney or law student;
• Be a member of the ABA;
• Be under age 40 at the time of the nomination;
• Either have published a recent article on a bankruptcy related topic in an ABA sponsored publication or have produced a significant report, study, or other work product in conjunction with service on the ABA Business Bankruptcy Committee, a subcommittee of the ABA Business Bankruptcy Committee, or task force of the ABA Business Bankruptcy Committee;
• Have demonstrated leadership potential within the ABA or the larger legal community; and
• Have displayed generosity of spirit.