

Agenda G-7
Rules of Practice
and Procedure
March, 1985

SUMMARY

REPORT OF THE JUDICIAL CONFERENCE COMMITTEE ON RULES OF PRACTICE AND PROCEDURE

This report contains the following recommendation:

That the Conference approve the proposed amendments to Bankruptcy Rules 5002 and 5004 and transmit them to the Supreme Court for its consideration with a recommendation that they be approved by the Court and transmitted to Congress pursuant to law.



**REPORT OF THE JUDICIAL CONFERENCE
COMMITTEE ON RULES OF PRACTICE AND PROCEDURE**

TO THE CHIEF JUSTICE OF THE UNITED STATES, CHAIRMAN, AND
MEMBERS OF THE JUDICIAL CONFERENCE OF THE UNITED STATES:

Your Committee on Rules of Practice and Procedure has not met since the last session of the Conference. We have, however, corresponded concerning the proposed amendments to the Bankruptcy Rules and the chairman of the Committee attended the last meeting of the Advisory Committee on Bankruptcy Rules when the proposed amendments were considered.

I. Rules of Bankruptcy Procedure

The Advisory Committee on Bankruptcy Rules has submitted to your Committee proposed amendments to Bankruptcy Rules 5002 and 5004. These proposed amendments are set out in Appendix A and are accompanied by Committee Notes explaining their purpose and intent. A separate report from the Chairman of the Advisory Committee summarizes the Advisory Committee's work.

At the September, 1984 session the Conference authorized the submission of these proposed amendments to the Executive Committee of the Conference. Because of a delay in processing them through the Advisory Committee and the Standing Committee, submission to the Executive Committee was not possible. Your Committee recommends that these proposed amendments be approved by the Conference and transmitted to the Supreme Court for its consideration with a recommendation that they be approved by the Court and transmitted to the Congress pursuant to law.

**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 COMMITTEE ON RULES OF PRACTICE AND PROCEDURE:

I have the honor of submitting herewith our Committee's final draft of proposed amendments to Bankruptcy Rules 5002 and 5004 with the recommendation that they be approved and presented to the Judicial Conference of the United States for action by that body.

Except for an amendment to subsection (a) of Rule 5004, these proposed amendments were widely circulated to the bench and bar for comment in August, 1984 and were also printed by the West Publishing Company in the various advance sheets of the National Reporter System. Written comments were requested to be filed by January 1, 1985. Public hearings were also scheduled to be held in Washington, D. C. on January 17, 1985, but were cancelled because there was no request for an opportunity to testify.

At its meeting on January 31, 1985 the Committee reviewed the comments received, which were few in number. Only one correspondent thought that the rules should not be amended. Support for the proposed amendments by correspondents and Committee members was overwhelming.

During its deliberations the Advisory Committee noted a problem with the language of subsection (a) of Bankruptcy Rule 5004 which currently reads as follows:

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

The Bankruptcy Code enacted in 1978 clearly made bankruptcy judges subject to the disqualification statute, 28 U.S.C. § 455, by including them within the definition of a judge contained in 28 U.S.C. § 451. The Bankruptcy Amendments and Federal Judgeship Act of 1984, however, raises a question as to whether a bankruptcy judge is now subject to the disqualification statute. To eliminate this ambiguity the Advisory Committee is recommending an amendment to Bankruptcy Rule 5004(a) to make it clear that Section 455 does apply. While this proposal has not been circulated to the bench and bar for comment, the Committee believes it is not controversial and that the proposed amendment is highly desirable.

We commend these changes to Bankruptcy Rules 5002 and 5004 set out in the attached schedule to the full Committee on Rules of Practice and Procedure and recommend approval.

Respectfully submitted,

Morey L. Sear
*Chairman of the Advisory
Committee on Bankruptcy Rules*

February 6, 1985

**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 § 402 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 individual may
16 be appointed as a trustee or examiner or be employed as an
17 attorney, accountant, appraiser, auctioneer, or other professional
18 person pursuant to § 327 or § 1103 of the Code if the individual is a
19 relative of the bankruptcy judge making the appointment or
20 approving the employment. Whenever under this subdivision an
21 individual is ineligible for appointment or employment, the
22 individual's firm, partnership, corporation, or any other form of
23 business association or relationship, and all members, associates and
24 professional employees thereof are also ineligible for appointment or
25 employment.

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

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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 A bankruptcy judge shall be governed
3 by 28 U.S.C. § 455, he and when disqualified from acting
4 thereunder, shall disqualify himself from presiding over the
5 adversary proceeding or contested matter in which the
6 disqualifying circumstance arises or, if appropriate, he shall
7 disqualify himself from presiding over the case.

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

COMMITTEE NOTE

Subdivision (a) was affected by the Bankruptcy Amendments and Federal Judgeship Act of 1984, P.L. 98-353, 98 Stat 333. The

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1978 Bankruptcy Reform Act, P.L. 95-598, included bankruptcy judges in the definition of United States judges in 28 U.S.C. § 451 and they were therefore subject to the provisions of 28 U.S.C. § 455. This was to become effective on April 1, 1984, P.L. 95-598, § 404(b). Section 113 of P.L. 98-353, however, appears to have rendered the amendment to 28 U.S.C. § 451 ineffective. Subdivision (a) of the rule retains the substance and intent of the earlier draft by making bankruptcy judges subject to 28 U.S.C. § 455.

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