BANKRUPTCY LITIGATION – USING THE FRUITS OF BANKRUPTCY RULE 2004 DISCOVERY IN CONTESTED MATTERS AND ADVERSARY PROCEEDINGS

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Bankruptcy Rule 2004[1] is a great tool to gain information concerning a debtor's pre-petition financial and business affairs. The results of Bankruptcy Rule 2004 discovery often leads to information which serves as the basis for filing a contested matters (*e.g.*, objections to exemptions) or adversary proceedings (*e.g.*, objections to discharge or the dischargeability of debts and challenges to the validity, extent and priority of liens). However, all too often, there is push back from Courts and opposing counsel to admitting the fruits of Bankruptcy Rule 2004 discovery into evidence. This reluctance is misplaced and begs the need to revisit the underpinnings of and justifications for admitting Bankruptcy Rule 2004 discovery into evidence.

A. Scope of Bankruptcy Rule 2004

Bankruptcy Rule 2004 provides, in pertinent part:

> (a) EXAMINATION ON MOTION. On motion of any party in interest, the court may order the examination of any entity.
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> (b) SCOPE OF EXAMINATION. The examination of an entity under this rule or of the debtor under § 343 of the Code may relate only to the acts, conduct, or property or to the liabilities and financial condition of the debtor, or to any matter which may affect the administration of the debtor's estate, or to the debtor's right to a discharge. In a family farmer's debt adjustment case under chapter 12, an individual's debt adjustment case under chapter 13, or a reorganization case under chapter 11 of the Code, other than for the reorganization of a railroad, the examination may also relate to the operation of any business and the desirability of its continuance, the source of any money or property acquired or to be acquired by the debtor for purposes of consummating a plan and the consideration given or offered therefor, and any other matter relevant to the case or to the formulation of a plan.
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> (c) COMPELLING ATTENDANCE AND PRODUCTION OF DOCUMENTS. The attendance of an entity for examination and for the production of documents, whether the examination is to be conducted within or without the district in which the case is pending, may be compelled as provided in Rule 9016 for the attendance of a witness at a hearing or trial. As an officer of the court, an attorney may issue and sign a subpoena on behalf of the court for the district in which the examination is to be held if the attorney is admitted to practice in that court or in the court in which the case is pending.

What discovery is permitted under Bankruptcy Rule 2004? On its face, Bankruptcy Rule 2004 permits "examination of any entity."[2] It does not specifically provide for paper discovery – e.g., interrogatories, requests for production, and requests for admission – *per se*, although subsection (b) provides that Bankruptcy Rule 9016 may be used to compel the attendance of an examinee and "the production of documents."[3] But is that a limitation? Traditionally, the production of documents is sought in connection with an oral examination.[4] But does the rule preclude interrogatories or requests for production? Not necessarily.

Neither Bankruptcy Rule 2004 nor the Bankruptcy Code define the term "examination." Black's Law Dictionary defines "examination" generally to mean interrogation of a witness.[5] Logic dictates that a person or entity could, technically, be "examined" in different contexts. Merriam Webster Dictionary defines "examination" to mean "a close and careful study of someone or something."[6] Therefore, the term "examination" would appear to include discovery tools such as interrogatories, requests for inspection of property, and requests for production of document and things.

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Six Bankruptcy Cases Granted Certiorari Before The United States Supreme Court In 2014
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52 *Petition*, at 4-5.
53 *Petition,* at 5-6.
54 *Petition*, at 6.
55 *Viegelahn v. Harris (In re Harris)*, 491 B.R. 866, 876 (W.D. Tex. 2013).
56 V*iegelahn v. Harris (In re Harris)*, 757 F.3d 468, 481 (5th Cir. 2014).
57 *Viegelahn,* 757 F.3d at 473.
58 *Id*. at 477.
59 *In re Michael*, 699 F.3d 305 (3d Cir. 2012)
60 *Michael,* 699 F.3d at 316.
61 *Id*., at 310.
62 No. 13-1421, 2014 WL 2207208 (U.S. Nov. 17, 2014); appealed from *Bank of Am., NA v. Caulkett (In re Caulkett)*, 566 Fed. Appx. 879 (11th Cir, Mem. Op.).
63 No. 14-163, 2014 WL 3965212, at *1 (U.S. Nov. 17, 2014); appealed from *Bank of Am., NA v. Toledo-Cardona (In re Toledo-Cardona)*, 556 F. App'x 911 (11th Cir. 2014).
64 *McNeal vv. GMAC Mortg.., LLC (In Re McNeal)*, 735 F.3d 1263, 1265-66 (11th Cir. 2012).
65 *Folendore v. United States Small Bus. Admin.*, 862 F.2d 1537 (11th Cir.1989).
66 *Caulkett*, 566 F. App''x at 880.
67 *Id*.
68 *Id*.
69 *Toledo-Cardona*, 556 F. App'x at 912.
70 *Supra*.
71 *Supra.*
72 *Dewsnup v. Timm*, 502 U.S. 410, 112 S.Ct. 773, 116 L. Ed. 2d 903 (1992).
73 *Toledo-Cardona*, 556 F. App'x at 912; *Dewsnup*, 502 U.S. at 417, 112 S. Ct. at 778.
74 *Toledo-Cardona*, 556 F. App'x at 912.
75 *Ryan v. Homecomings Financial Network (In re Ryan)*, 253 F.3d 778, 782-83 (4th Cir. 2011).
76 *Talbert v. City Mortgage Services, (In re Talbert)*, 344 F.3d 555, 561 (6th Cir. 2012).
77 *Palomar v. First Am. Bank, (In re Palomar)*, 722 F.3d 992, 993-94 (7th Cir. 2013).
78 *Brief in Opposition, Bank of Am, NA v. Caulkett*, No. 13-1421, 2014 WL 5077231 at *8 (U.S. Appellate Petition, Oct. 6, 2014).
79 *Id*. at *9.
80 *Bank of Am., N.A. v. Sinkfield*, 134 S. Ct. 1760, 188 L. Ed. 2d 593 (2014).
81 *Brief in Opposition*, 2014 WL 5077231 at *7.

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Further, while Bankruptcy Rule 2004 provides that the scope of examination "may relate only to the acts, conduct, or property or to the liabilities and financial condition of the debtor, or to any matter which may affect the administration of the debtor's estate, or to the debtor's right to a discharge,"[7] courts have held that discovery under Bankruptcy Rule 2004 is broader than that typically permitted under the Federal Rules of Civil Procedure,[8] amounting to a "lawful fishing expedition."[9] One would presume that this breadth of scope would include the tools necessary as a means to that end. Of course, this breadth is precisely why counsel for the respondents/defendants in contested matters/adversary proceedings frequently object to the use of Bankruptcy Rule 2004 discovery in evidentiary hearings/trials.

B. Contested Matters Versus Adversary Proceedings

The advisory committee notes accompanying Bankruptcy Rule 9014 provide: "Whenever there is an actual dispute, other than an adversary proceeding…the litigation to resolve that dispute is a contested matter."[10] An adversary proceeding," on the other hand, is a *lawsuit* filed within the bankruptcy case.[11]

Discovery in contested matters is governed by Bankruptcy Rule 9014(c), which provides:

> (c) APPLICATION OF PART VII RULES. Except as otherwise provided in this rule, and unless the court directs otherwise, the following rules shall apply: 7009, 7017, 7021, 7025, 7026, 7028–7037, 7041, 7042, 7052, 7054–7056, 7064, 7069, and 7071. The following subdivisions of Fed. R. Civ. P. 26, as

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> incorporated by Rule 7026, shall not apply in a contested matter unless the court directs otherwise: 26(a)(1) (mandatory disclosure), 26(a)(2) (disclosures regarding expert testimony) and 26(a)(3) (additional pre-trial disclosure), and 26(f) (mandatory meeting before scheduling conference/discovery plan). An entity that desires to perpetuate testimony may proceed in the same manner as provided in Rule 7027 for the taking of a deposition before an adversary proceeding. The court may at any stage in a particular matter direct that one or more of the other rules in Part VII shall apply. The court shall give the parties notice of any order issued under this paragraph to afford them a reasonable opportunity to comply with the procedures prescribed by the order.

Bankruptcy Rule 7001 addresses discovery in adversary proceedings, providing, in part, that "[a]n adversary proceeding is governed by the rules of this Part VII."[12] Part VII includes, by reference therein, the discovery rules in the Federal Rules of Procedure that apply to adversary proceedings. Bankruptcy Rule 2004 is not mentioned in either of these rules. Query: Does the omission constitute a statement on admissibility?

C. Bankruptcy Rule 2004 Discovery Should Be Admissible In Contested Matters And Adversary Proceedings

Bankruptcy Rule 2004 discovery should be admissible in merit proceedings involving contested matters and adversary actions – this includes dispositive motions (*e.g.*, summary judgment), final hearings, and trials.

In dispositive motion practice, as with hearings and trials on the merits, evidentiary submissions are premised on the Federal Rules of Civil Procedure. For example, Rule 56 of the Federal Rules of Civil Procedure, adopted for application in contested matters and adversary proceedings, provides that a fact can be established by

> citing to particular parts of materials in the record, including depositions, documents, electronically stored information, affidavits or declarations, stipulations (including those made for the purposes of the motion only), admissions, interrogatory answers, or other materials.[13]

(emphasis added) Fed. R. Civ. P. 56(c)(1)(A).

Dispositive motions equate effectively to trials on the merits. While the standards of review applied by a court in evaluating such motions may be different from those at a final hearing or trial – *e.g.*, whether or to what extent claims have been well-pled and/or are plausible and whether there are genuine issues of material fact in dispute versus whether claims have been established by a preponderance of the evidence – the evidentiary analyzes are the essentially same.

1. Use of Bankruptcy Rule 2004 Testimony In Support of Dispositive Motions

While, technically, testimony given in a Bankruptcy Rule 2004 deposition may not qualify as a "deposition" taken under Federal Rule 30 that can be used as evidence under Rule 56(c)(1)(A), the testimony does frequently qualify and has the same reliability as an affidavit under the same provision.[14] Bankruptcy Rule 2004 examination testimony satisfies the requirements of Rule 56(c)(4) in that it is made on personal knowledge, sets out facts that would be admissible in evidence, and demonstrates that the declarant is competent to testify on the matters therein. In short, "[c]ertified testimony complying with Rule 56(e)...has the same evidentiary value and safeguards as affidavits provided for in Rule 56(e), supra, which do not afford an opportunity for cross-examination."[15]

The Ninth Circuit Court of Appeals addressed this issue directly in the case of *Hoover v. Switlik Parachute Co.*[16] In *Hoover*, plaintiff sued for injuries sustained while using a parachute. After certain depositions were taken in discovery, defendants Pioneer and Switlik were added as defendants.[17] Pioneer filed for summary judgment relying on deposition testimony taken before either it or Switlik Parachute Co. were parties.[18] Switlik argued that the depositions were not admissible because it did not have an opportunity to cross-examine the deponents.[19] On appeal, the Ninth Circuit Court of Appeals ruled that even though the depositions would not be admissible at summary judgment as depositions, they were still admissible as affidavits because they meet all the same qualifications under Rule 56.[20]

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Bankruptcy Rule 2004 testimony meets the requirements of an affidavit under Rule 56 and, therefore, should be admissible. If the other side disagrees with the testimony or evidence presented in connection with a motion for summary judgment they can assert or claim so with controverting summary judgment evidence which attempts to demonstrate an inability of the movant to recover on and controverts the very basis of its claims.

2. Other Bases For Permitting Introduction of Bankruptcy Rule 2004 Testimony

There are other numerous, sound arguments for the allowance of Bankruptcy Rule 2004 testimony at evidentiary hearing/trials of contested matters and adversary actions.

(a) Residual Hearsay Exception

Bankruptcy Rule 2004 testimony should be admissible under Rule 807 of the Federal Rules of Evidence,[21] the residual hearsay exception, which is adopted for application in both contested matters and adversary proceedings.[22] Rule of Evidence 807 provides that a hearsay statement that does not fall under Rules of Evidence 803 or 804 is still admissible, if:

a. The statement has equivalent circumstantial guarantees of trustworthiness;
b. It is offered as evidence of a material fact;
c. It is more probative on the point for which it is to be offered than any other evidence that the proponent can obtain through reasonable means; and
d. Admitting it will best serve the purposes of these rules and the interests of justice.

In *Johnson v. Nelson (In re Slatkin)*[23] the trustee filed an adversary proceeding against investors to recover fraudulent transfers of purported profits from the debtor's Ponzi scheme. The court held that the debtor's plea agreement filed in his criminal action was admissible at summary judgment under the Rule 807 residual exception to hearsay in order to prove that the debtor was involved in a Ponzi scheme.[24] The court held that the plea agreement where the debtor admitted he operated a Ponzi scheme was the most probative evidence on the issue, that it covered a material fact, had equivalent circumstantial guarantees of trustworthiness and furthered the general purposes of the rules of evidence.[25]

(b) Admission of a Party Opponent

Bankruptcy Rule 2004 testimony may also be deemed to constitute an admission of a party opponent under Rule 801(d)(2) of the Federal Rule of Evidence.[26] In *In re McLaren*[27] a creditor brought a claim against a chapter 7 debtor pursuant to 11 U.S.C. § 523(a).[28] At trial, the debtor chose not to testify and the creditor moved to admit portions of the debtor's Bankruptcy Rule 2004 examination testimony.[29] Acknowledging that Bankruptcy Rule 2004 examinations provide fewer protections than Rule 30 of the Federal Rules of Civil Procedure, the court held that the testimony was nevertheless admissible into evidence because the circumstances surrounding the taking of the examination provided the debtor with ample notice that the information was important to the creditor's case and that it would be used accordingly.[30]

(c) Witness Unavailability

Bankruptcy Rule 2004 testimony may also be admissible where the witness is unavailable to testify at trial in accordance with Rule 32(a)(4) of the Federal Rules of Civil Procedure and Rule 804 of the Federal Rules of Evidence.[31] In *Samson v. W. Capital Partners LLC (In re Blixseth)*,[32] a creditor examined a witness during a Bankruptcy Rule 2004 deposition prior to the commencement of an adversary proceeding.[33] When called to testify at trial, the witness refused to testify by invoking the Fifth Amendment.[34] The court distinguished the situation at bar from those where movants seek to circumvent the Federal Rules of Civil Procedure and held that the examination transcripts were admissible despite defendant's hearsay objections.[35]

(d) Waiver

Finally, if the other party was on notice of the proponent's intention to use the Bankruptcy Rule 2004 evidence and makes

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no objection, it could be said that they have waived any argument against the admissibility of the evidence at a hearing or trial. For example, if the Bankruptcy Rule 2004 discovery is used to support a motion for summary judgment or other evidence based pre-trial motion, without objection, why should the party later be permitted to object to its use at a final evidentiary hearing or trial on the merits? Similarly, if a party uses Bankruptcy Rule 2004 discovery to rebut an argument made by the other side or to controvert evidence placed before the Court, that party should not later be heard to argue that Bankruptcy Rule 2004 evidence is inadmissible, if the evidence is otherwise relevant to the issues before the Court.

D. Practice Tips

Because Bankruptcy Rule 2004 discovery is conducted in a vacuum and there is no way to determine whether the fruits of the examination will result in support for action to be taken, the examination should be approached as if it will be used in collateral proceedings. The following tips should be considered:

- In your motion to conduct discovery pursuant to Bankruptcy Rule 2004, note that you reserve the right to serve interrogatories, requests for production, depositions on written questions, as well as notices for oral deposition. Have the order provide that these discovery vehicles are available.

- Make sure the Bankruptcy Rule 2004 examination has as many *indicia* of an oral deposition under Federal Rule 30 as possible. To accomplish this, the target of a request for a Bankruptcy Rule 2004 examination should be *Mirandized* as to the intended scope and application of the deposition. Make clear that it is your intention that the fruits of the examination will be used to evaluate whether motions, objections and/or adversary actions may be filed. Broadcast this intention in the notice of and on the record at the beginning of the Bankruptcy Rule 2004 deposition. This will support a waiver argument later when the testimony is sought to be used.

- If you believe or have reason to believe that the debtor or other persons or entities may be targets of an action based on Bankruptcy Rule 2004 discovery, be sure to specifically notice and invite them to attend and ask questions. Make it clear on the record who is in attendance and that will be given an opportunity to examine the witness.

- Consider asking counsel in attendance if they will stipulate on the record at the Bankruptcy 2004 examination that the testimony and documents produced may be used in collateral proceedings.

- After the contested matter or adversary proceeding has been filed, ask counsel for the respondent/defendant whether they will stipulate to using Bankruptcy Rule 2004 discovery in the proceedings. If so, prepare and file a stipulation in the case or adversary proceeding to this effect. If they will not agree to do so, consider sending the respondent/defendant an interrogatory and/or a request for admission asking that they agree that the testimony provided in the Bankruptcy Rule 2004 deposition (as attached to the interrogatory or request for admission) is the truthful, correct, genuine, authentic, accurate testimony of the person or entity involved. This will force them to either admit the authenticity and admissibility or explain why they cannot do so and take steps to prove otherwise. If they cannot admit the request, the court can be asked to opine on the matter or the deposition can be retaken if necessary and the transcript marked as an exhibit. If they admit, then the burden will be on them to gain controverting testimony or other evidence.

- Make sure the transcription of Bankruptcy Rule 2004 testimony is certified by the court reporter and the other side has had an opportunity to review it and sign it before a notary and make any corrections to an *errata* page. On the record, indicate that you will be requesting a transcript and the review and signature of the deponent; otherwise, unless there is an objection, you will be permitted to use a certified copy of the original, unsigned testimony in lieu of the signed original in any further proceedings.

- Finally, consider designating the target of the Bankruptcy Rule 2004 examination as witness for hearing/trial. If required, designate specific pages and lines of the transcript. If exhibits used in the examination are desired to be used at the hearing/trial, separately designated as exhibits for the hearing/trial, as well as referencing them as an

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exhibit to the examination. In most districts, counsel is required to state objections to exhibits in advance of hearing/trial. If there is no objection, move for admission of the exhibit at the being of the hearing/trial and argue waiver of any objection.

E. Conclusion

Bankruptcy Rule 2004 is a great tool to gather information that may lead to the filing of contested matters and adversary proceedings. Taking steps beforehand to strengthen the right to use the fruits of such discovery will save time and money in the event the information proves beneficial to establishing your claims and causes of action.

The foregoing is presented for educational purposes only and should not be relied upon as legal advice. Although prepared by professionals, it should not be utilized as a substitute for professional services in specific situations. If legal advice or other expert assistance is required, the services of a professional should be sought.

ENDNOTES

1 Fed. R. Bankr. P. 2004 (**"Bankruptcy Rule 2004"**).
2 "Entity," is defined in the Bankruptcy Code to include "person, estate, trust, governmental unit, and United States trustee." 11 U.S.C. § 101(15).
3 Bankruptcy Rule 9016 provides: "Rule 45 Fed. R. Civ. P. applies in cases under the Code."
4 And, as will be noted, because a Bankruptcy Rule 2004 examination is not one taken under the Federal Rules of Civil Procedure, the temporal limitations in Federal Rule of Civil Procedure 30 and 34 (30 days to produce) do not apply to a request for production in connection with an notice of examination under Bankruptcy Rule 2004.
5 *See* Black's *Law Dictionary* (4th ed. 1968).
6 *See* www.merriam-webster.com.
7 Fed. R. Bankr. P. 2004(b).
8 Bankruptcy Rule 2004 affords both debtors and creditors broad rights of examination of a persons and entities with respect to the business and financial affairs of the debtor and administration of the estate. However, its scope is not limitless. For example, examinations cannot be used to harass or oppress the party and should not be used to obtain information for use in an unrelated case or proceeding pending before another tribunal. *In re Snyder*, 52 F.3d 1067 (5th Cir. 1995) (citations omitted). Under the Federal Rules of Civil Procedure, discovery is generally limited to information which is relevant to the claims asserted or is likely to lead to the discovery of relevant information. *See* Fed. R. Civ. P. 26(b)(1).
9 *See In re Bounds*, No. 09–12799, 2010 WL 3447683, at *5–6, 2010 Bankr. LEXIS 2983, at *14 (Bankr. W.D.Tex., August 31, 2010) (noting that numerous courts have likened a Bankruptcy Rule 2004 examination to a fishing expedition). *See also In re NE 40 Partners, Ltd. Partnership*, 440 B.R. 124, 129 (Bankr. S.D. Tex. 2010) ("[T]he discovery tools available to a creditor or trustee Chapter 7 trustee should allow a trustee to present the "who, what, where, when, and how," thus forcing trustees to do their homework before filing an adversary proceeding and subsequently improving judicial economy" citing *Benchmark Elecs.*, 343 F.3d at 724 (5th Cir.2003).").
10 Fed. R. Bankr. P. 9014, Advisory Committee Notes.
11 Fed. R. Bankr. P. 7001. *See also* 10 Collier on Bankruptcy ¶ 7001.01 (Alan N. Resnick & Henry J. Sommer eds., 16th ed. 2010) ("Adversary proceedings are separate lawsuits within the context of a particular bankruptcy case and have all the attributes of a lawsuit...."). Adversary proceedings are initiated with the filing of a complaint. Fed. R. Bankr. P. 7003; Fed. R. Civ. P. 3.
12 Fed. R. Bankr. P. 7001 (**"Bankruptcy Rule 7001"**).
13 (emphasis added) Fed. R. Civ. P. 56(c)(1)(A). Fed. R. Bankr. P. 7056 and 9014.
14 *See Menotte v. Leonard (In re Leonard)*, 418 B.R. 477 (S.D. Fla. 2009) (holding that the transcript of a Rule 2004 examination is admissible as a transcript under Rule 56(c) of the Federal Rules of Civil Procedure because it was "made with personal knowledge and set forth facts in evidence.").
15 *Steven v. Roscoe Turner Aeronautical Corp.*, 324 F.2d 157, 162 (7th Cir. 1963); *see also Shulins v. New England Insurance Co.*, 360 F.2d 781 (2nd Cr. 1966) (holding that the certified transcript of a court record was admissible as evidence at summary judgment).
16 663 F.2d 964 (9th Cir. 1981).
17 *Id.* at 966.
18 *Id.*
19 *Id.*
20 *Id.*
21 Fed. R. Evid. 807.

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22 *See* Fed. R. Bankr. P. 9017.

23 525 F.3d 805 (9th Cir. 2008).

24 *Id.* at 812.

25 *Id. Cf. Roberts v. Oliver (In re Oliver)*, 414 B.R. 361, 371 (Bankr. E.D. Tenn. 2009). Arguably, *Oliver* is limited to its facts and procedural situation. Most significant, however, is that the court in *Oliver* does not address or consider whether testimony given in a Bankruptcy Rule 2004 examination is admissible as an affidavit under Rule 56.

26 Fed. R. Evid. 801(d)(2). Federal Rule of Evidence 801(d)(7) provides that a statement made by a party is not hearsay if:

> The statement is offered against an opposing party and
>
> 1. Was made by the party in an individual or representative capacity;
> 2. Is one the party manifested that it adopted or believed to be true;
> 3. Was made by a person whom the party authorized to make a statement on the subject;
> 4. Was made by the party' agent or employee on a matter within the scope of that relationship; or
> 5. Was made by the party's coconspirator in furtherance of the conspiracy

27 3 F.3d 958, 964 (6th Cir. 1993).

28 *Id.* at 959.

29 *Id.*

30 *Id.* at 964.

31 Fed. R. Civ. P. 32(a)(4); Fed. R. Evid. 804.

32 489 B.R. 154, 181 (Bankr. D. Mont. 2013).

33 *Id.* at 182.

34 *Id.*

35 *Id. See also In re Avon Townhomes Venture*, 433 B.R. 269, 280 n. 13 (Bankr. N.D. Cal. 2010).