AIRA Association of Insolvency & Restructuring Advisors

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# ISSUES AND PITFALLS RELATING TO THE RETENTION OF FINANCIAL ADVISORS, RESTRUCTURING CONSULTANTS AND ACCOUNTANTS

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*Duane Morris LLP*

The United States Bankruptcy Code (the "Code")[1] and the Bankruptcy Rules (the "Rules")[2] set forth the manner in which professionals who seek to be retained by a Trustee, Creditors Committee or a Debtor must operate. Section 327(a) of the Bankruptcy Code provides:

> The trustee, with the court's approval, may employ... professional persons, that do not hold or represent an interest adverse to the estate, and that are disinterested persons, to represent or assist the trustee in carrying out the trustee's duties under this title.

11 U.S.C. § 327(a).

**Disclosure Under Bankruptcy Rule 2014:**

Rule 2014, provides, in pertinent part:

> The application shall state the specific facts showing_the necessity for the employment, the name of the person to be employed, the reasons for the selection, the professional services to be rendered, any proposed arrangement for compensation, and, to the best of the applicant's knowledge, all of 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 application shall be accompanied by a verified statement of the person to be employed setting forth 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.

When a trustee, debtor or creditors committee seeks to hire a professional, an employment retention application must reveal all connections between the professional and the debtor, the creditors and any other party of an interest, including the case trustee and the United States trustee, as well as any connection that may exist between the professional and any accountant or attorney for the debtor, a creditor, or other party of interest. In determining whether there has been compliance with the requirements of Rule 2014(a) it is the degree of completeness of the disclosure, rather than the applicants' subjective intent or state of mind with respect to disclosure, that is material. *See In Re Begun*, 162 B.R. 168 (Bankr. N.D. 1ll. 1993).

Failure to disclose a connection with a party of interest is sanctionable. Even a negligent or inadvertent failure to fully disclose relevant information may result in denial of all requested fees. *In Re Park-Helena Corp.*, 63 F.3d 877 (9th Cir. 1995) *Cert. denied*, 516 U.S. 1049 (1996).

Rule 2014 and Code §327 mandate disclosure of potential as well as actual conflicts of interest. *Hansen, Jones, Leta, PC v. Segal* 220 B.R, 434 (D. Utah 1998). Although Rule 2014 does not expressly require supplemental or continuing disclosure, Code §327 (a) implies a duty of continuing disclosure. Near boiler plate statements disclosing perspective connections is rarely satisfactory. *See In Re Granite Partners, LP* 219 B.R. 22 (Bankr. S.D.N.Y. 1998).

It is not left to the discretion of the professional to pick and choose those connections which they deem relevant to disclose; rather they must disclose all facts that bare on the issue of disinterestedness. *In Re Granite Partners*, 219 B.R. at 35. Applicants and their professionals must strictly comply with Rule 2014. Failure to disclose all connections provides a basis to disallow fees and even disqualify the professional. *See In Re Leslie Fay*, 175 B.R. 525 (Bankr. S.D.N.Y. 1995). The Court in *Leslie Fay* noted: "the requirements of Fed. R. Bankr. P. 2014 are more-encompassing then those governing the disinterestedness inquiry under §327. For a while retention under §327 is only limited by

1 All references to the "Code" refer to 11 U.S.C. §§101 et al., as amended.

2 All the reference to the Bankruptcy Rules refer to Fed. R. Bankr. P. 101 et al., as amended.

***Pitfalls*** continues on **Page 12**

## *IN THIS ISSUE*

# Letter from the Executive Director

*Grant Newton, CIRA*
*AIRA*

For the last several months I have been working on a basic bankruptcy course that will be available in March for both Self and Group Study. This will expand the AIRA's offerings for professional education, providing a comprehensive yet flexible program to meet a variety of situations and objectives. The course consists of eight parts as follows:

Chapter 1: Nature of the Bankruptcy Process
Chapter 2: Preplanning for and Filing of the Petition
Chapter 3: Issues Related to Operating and Turning Around Troubled Businesses
Chapter 4: Creditor Rights and Claims
Chapter 5: Financial Reporting During Chapter 11 (FASB ASC 852)
Chapter 6: Chapter 11 Plans
Chapter 7: Reporting Requirements Under FASB ASC 852 on Emergence from Chapter 11
Chapter 8: Special Situations Involving Financial Advisors in Recovery Action (such as preferences and fraudulent transfers; forensic accounting)

The group study course includes an instructor's guide with teaching suggestions, PowerPoint slides, exercises and study questions with suggested solutions. The group course is recommended for 5-25 participants.

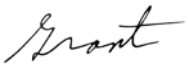
The self study course is offered as separate modules wherein the participant may register separately for each chapter (Chapters 1-8) or for all eight chapters at once (complete course). Each module completed qualifies for one hour of CPE credit and the complete course qualifies for 8 units of CPE credit.

In Memoriam: Robert Morris

We regret to report that Board of Director member and respected professional associate, Robert Morris, passed away on Saturday, February 20. For many years, Bob was a strong and valued supporter, an important contributor to both the AIRA and CIRA program. He exemplified the Association's objectives and standards and served them for many years, holding both CIRA and CDBV certificates and co-chairing the 2007 Annual Conference in Chicago. Bob worked with MorrisAnderson for the last 12 years, leaving his position recently after being diagnosed with pancreatic cancer last Fall. In addition to his efforts for AIRA, he was also very active as member of TMA. His contributions to the profession spanned an extended time period and impacted many: we have lost a good friend and colleague.

As we enter the final weeks of preparation for AIRA's 26th Annual Conference in the incredible San Diego, California, setting, I look forward to seeing and working with you in June (see AIRA's website for conference information and registration).

Best regards,



# Bankruptcy Retakes

*Professor Jack F. Williams, CIRA/CDBV*
*Georgia State University*

## On Ethics

As we begin 2010, I wanted to share with you the subject matter of several recent calls to me by fellow members. These calls focused on ethics in the restructuring profession. All callers were AIRA and CIRA members; thus, any potential ethics issue must be addressed initially by application of our own Code of Professional Ethics (Code) and any other body of ethics that may regulate any other professional certification one may possess. You may find our Code on the AIRA website and in the front of our directory.

Our Code begins with a general statement: "AIRA members and holders of CIRA and CDBV certification are expected to exemplify the highest standards of professional ethics . . . ." Our professional ethics center on the attributes of competence, confidentiality, integrity, objectivity, and due care. I want to address the attributes of competence and due care. At the outset, our Code demands that we apply our knowledge and skill with reasonable care and diligence maintain an appropriate level of professional competence by continuing to develop knowledge and skills. Moreover, the Code requires that we perform professional duties in accordance with the law, regulations, or any technical standards. Our Code then cautions us not to take engagements for which we do not have, nor can we reasonably acquire, the competence to complete.

Along with the requirement that we conduct ourselves competently, our Code mandates that we discharge our professional responsibilities with competence and diligence. Due care further includes that we adequately plan and supervise our performance of professional services. Finally, the Code requires that we obtain sufficient relevant data to afford a reasonable basis for conclusions or recommendations in relation to any professional services performed.

In summary, the requirements of competence and due care require that we exercise the care that a person in a like position would exercise under similar circumstances. That requires that we accept engagements that we have the competence to handle or reasonably believe that we can acquire the skills or retain the consultants to handle competently. This is especially important where a CIRA is asked to conduct a solvency analysis under the Bankruptcy Code where certain asset or liability classes require technical skills or experience to value or determine, respectively, that most CIRAs would not have. Furthermore, these requirements insist that we continue to participate in meaningful continuing education. In difficult financial times, many of us cut back our budget on CPE programs. That is short-sighted. Our professional world is changing dramatically and at warp speed. We must improve both the breadth and depth of our skills. Now is not the time to cut educational corners.

In my next column, I plan to address the remaining etihcs requirements.