Cullen | Dykman

Bankruptcy Rule 2004: The Broad Sweep of Discovery Permitted in Bankruptcy Litigation

March 26, 2021

Michael Traison
Chicago/NYC – 312.860.4230

Elizabeth Usinger
Garden City – 516.357.3869

Amanda Tersigni
Garden City – 516.357.3738

In American jurisprudence, resolution of disputes often involves the use of important tools to obtain information necessary to achieving a client's goals. These tools are collectively known as "discovery." Discovery is most often used in litigation; however, it may also be used as part of the bankruptcy process, without the need for a pending lawsuit.

In many respects, discovery is unique to the American legal system and rare in other countries in the same form. Types of discovery include depositions (examinations under oath), interrogatories (written questions), requests for production of documents and requests for admissions.

Generally, Rules 26 through 37 of the Federal Rules of Civil Procedure govern discovery in federal courts. Rule 26(b)(1) discusses the scope of such discovery and allows parties to obtain discovery of any nonprivileged matters relevant to any party's claim or defense. Even though the discovery need not be admissible in evidence to be discoverable, the federal rule itself contemplates a way to balance the type of discovery that is important for purposes of the case, while preventing unfettered discovery beyond what may be deemed relevant for a particular matter.

While each state's discovery rules may vary, the rules are relatively similar to the federal rules. For example, the New York Civil Practice Law and Rules encourage "full disclosure of all matter *material and necessary* in the prosecution or defense of an action." CPLR § 3101(a) (emphasis added).

Bankruptcy is different.

In bankruptcy cases, Rule 2004 of the Federal Rules of Bankruptcy Procedure permits broad discovery, as do other federal discovery rules which are incorporated from the Federal Rules of Civil Procedure. While the party seeking Rule 2004 discovery must show good cause for the examination it seeks, (*see In re Sunedison, Inc.*, 572 B.R. 482, 490 (Bankr. S.D.N.Y. 2017)), the scope of Rule 2004 is very broad and often referred to as a "fishing expedition."

A Rule 2004 examination, while essentially a form of deposition, is an examination of any person or entity who may have knowledge pertinent to discovery of assets and it is used to examine transactions, as well as to determine whether wrongdoing has occurred. *See In re Enron Corp.*, 281 B.R. 836, 840 (Bankr. S.D.N.Y. 2002); *see also In re Cambridge Analytica LLC*, 600 B.R. 750, 751 (Bankr. S.D.N.Y. 2019) (noting the scope of Rule 2004 examination relates to the acts, conduct, or property or to the liabilities and financial condition of the debtor, or anything else that impacts the debtor's estate). The examination can be conducted by any "party in interest," a term which is also broad. The purpose of Rule 2004 is to allow inquiry into matters that will affect the administration of the debtor's estate.

However, there are circumstances where the use of Rule 2004 will be limited, despite its otherwise broad and unfettered nature. *See In re Enron Corp.*, 281 B.R. at 840 (finding "the availability of Rule 2004 as a discovery tool is not unlimited"). Limitations have been imposed where the purpose of the examination is to abuse or harass. *See id*. Bankruptcy Courts have the discretion to determine whether the Rule 2004 discovery will be allowed and consider the competing interests of parties, balancing the relevance of and necessity of the information sought by the Rule 2004. *See In re Sunedison, Inc.*, 572 B.R. at 489-90.

Additionally, when there is an adversary proceeding pending or contested matters commenced, discovery should be pursued under the Federal Rules of Civil Procedure and not under Rule 2004. *See In re Enron Corp.* at 840-41 (finding that Rule 2004 should not be used as a tactic to circumvent the safeguard of the Federal Rules of Civil Procedure). The Federal Rules of Civil Procedure are generally more restrictive in scope.

Of course, a Rule 2004 examination is conducted under oath and penalty of perjury. The testimony elicited may also be used for other purposes in other proceedings. Thus, there are considerations of various privileges and protections that can be asserted throughout the examination, including protections of the Fifth Amendment, attorney-client privilege, and attorney work product.

Discovery has the potential of being prolonged and voluminous, so there are rules to restrain the proponent and maintain organization of the responses.

Nonetheless, the expense of discovery, and sometimes the implications for a client, may encourage settlement.

Please note that this is a general overview of developments in the law and does not constitute legal advice. Nothing herein creates an attorney-client relationship between the sender and recipient. If you have questions regarding these provisions, or any other aspect of bankruptcy law, please contact Michael Traison at 312.860.4230, Elizabeth Usinger 516.357.3869 or Amanda Tersigni at 516.357.3738.

Practices

- Bankruptcy and Creditors' Rights

Attorneys

- Michael H. Traison
- Elizabeth Usinger