

Bankruptcy Law

Bankruptcy Do's and Don'ts for Personal Injury Attorneys

Ease your pain with a useful road map for the system

By Timothy P. Duggan

The increase in consumer bankruptcy filings has caused many sleepless nights for personal injury lawyers as they contemplate navigating the United States Bankruptcy Code in order to determine how a client's bankruptcy case impacts a pending personal injury lawsuit. This article is intended to ease the pain and provide a road map for personal injury lawyers (primarily plaintiff's attorneys) in the form of a list of Dos and Don'ts.

Plaintiff Files For Bankruptcy Protection

A common scenario is when a plaintiff calls her personal injury lawyer and advises her that she has filed for bankruptcy protection. This call often comes well after the bankruptcy case is filed and sometimes on the eve of consummating a settlement of the personal injury case. What are the essential Dos and Don'ts?

Do be proactive and immediately call

Duggan is the chair of Stark & Stark's bankruptcy & creditor's rights group in Lawrenceville.

the client's bankruptcy counsel to determine when the bankruptcy case was filed, whether the personal injury action was disclosed on the bankruptcy schedules, and what type of bankruptcy was filed. As a general rule, if the accident occurred before the bankruptcy was filed, even if no lawsuit was filed, the case is property of the bankruptcy estate under Bankruptcy Code Section 541(a) and must be listed on the client's bankruptcy schedules (Schedule B). Once disclosed, you will need to determine who is the person that controls your decision making: your client or the bankruptcy trustee. In a Chapter 7 liquidation case, a Chapter 7 trustee steps into the shoes of a debtor and takes control of the personal injury action. In a Chapter 11 or Chapter 13 case filed by an individual, the debtor/plaintiff retains control over the personal injury action.

Do determine whether it is necessary to be retained as counsel and, if so, get retained. In order to represent a debtor or trustee in any type of litigation and be paid a legal fee from the bankruptcy estate, the attorney must be retained as special counsel. See Bankruptcy Code Section 327. In a Chapter 7 bankruptcy case, the trustee retains the personal injury lawyer. In a Chapter 11 or Chapter 13 case, the debtor retains the personal injury lawyer. In either event, an application must be filed with the bankruptcy court

and the bankruptcy judge must approve the retention. An exception to this rule is that in the event the Chapter 7 trustee determines that the personal injury case is of minimal or no value to the bankruptcy estate, the trustee can decide to abandon the personal injury case and return it to the debtor under Bankruptcy Code Section 554(a). Upon abandonment, the personal injury case is no longer subject to the control of the bankruptcy court and proceeds as if there was no bankruptcy case. If the case is abandoned, the personal injury lawyer does not need to be retained as special counsel.

Do make certain that any settlement is approved by the appropriate person and all necessary notices are filed with the bankruptcy court under Rule 9019 of the Federal Rules of Bankruptcy Procedure. As a general rule, all settlements must be approved by the bankruptcy court. Creditors are provided an opportunity to object to the settlement of a personal injury case. Also, it is very important to remember that in a Chapter 7 bankruptcy case, the trustee must approve a settlement in order for the settlement to be binding. The fact that the plaintiff is satisfied with the settlement is only part of the equation, since the trustee is the true party in interest. The notice procedures are not difficult, but will delay the ultimate settlement by 30 to 40 days.

Do note that your legal fee is subject to approval by the bankruptcy court. In order to be paid, special counsel must file an application for allowance of legal fees and expenses pursuant to Bankruptcy Code Section 330. The trustee or debtor's

counsel will generally prepare the application and cover sheet for special counsel. The application must set forth what the personal injury lawyer did to earn a fee and what benefit was provided to the bankruptcy estate.

Don't ignore the trustee's request for information about the personal injury case, especially at the outset of the bankruptcy case. One of the first decisions a trustee must make is whether to abandon the personal injury case. To make this decision, the trustee must be able to estimate the potential value of the case. It is very important to make complete disclosure of all facts that may help the trustee make her decision. Remember, in a Chapter 7 bankruptcy case, the trustee is your client.

Don't forget to advise defense counsel that any settlement is subject to approval by the trustee and the United States Bankruptcy Court. Trustees rarely reject a settlement recommended by special counsel, but it is a necessary step.

Don't ask why, just follow the rules. Is this process cumbersome? Yes. Does this process delay settlement of a case? Yes. Is it fair that a bankruptcy judge can award less than the contracted contingency fee after a case is completed? Take that one to Congress. Regardless of these answers, you cannot buck the system and any effort to circumvent the Bankruptcy Code or Bankruptcy Rules will jeopardize your legal fee and, in some cases, result in ethical issues. Trustees often complain that some personal injury lawyers simply refuse to keep them updated on a case, settle cases without bankruptcy court approval, and fight them on filing a fee application.

Don't be one of these lawyers. The trustees did not make the rules, but need to make certain they are followed.

Defendant Files for Bankruptcy Protection

Now that we have mastered the plaintiff's side of the ledger, what happens when a defendant in a personal injury case files for bankruptcy protection? The Dos and Don'ts that follow exclude issues that arise in mass-tort cases and are limited to cases that confront counsel on a day-to-day basis.

Do become familiar with the bankruptcy stay under Bankruptcy Code Section 362. The stay arises automatically and applies whether or not you know about the bankruptcy filing. Actions taken in violation of the bankruptcy stay are void and can subject the attorney to sanctions and damages.

Do get a copy of all insurance policies covering the accident or injury. As a general rule, a bankruptcy discharge does not let the insurance carrier off the hook. It is important to know what type of coverage exists, including whether there is any deductible or self-insured provision.

Do try to negotiate stay relief with the debtor or trustee, but remember the limits of any insurance policy. Many Chapter 7 trustees will consent to lift the bankruptcy stay if the plaintiff waives its claim against the bankruptcy estate and limits recovery to available insurance. Before making a decision to waive a claim, you must know if there is insurance coverage. If you cannot negotiate an order, you will need to file a motion with the bankruptcy court to obtain an order to lift the bankruptcy stay.

Do calendar the deadline to file a proof of claim. If this deadline is missed, read *Pioneer Inv. Servs. v. Brunswick Associates*, 507 U.S. 380 (1993) (excus-

able neglect standard).

Don't assume stay relief is always the way to go. If there is large self-insured retention in a larger retailer case, the debtor may ask the bankruptcy court to approve an alternate dispute resolution (ADR) procedure in order to handle the numerous personal injury and other types of unsecured claims. It is advisable to raise this issue when you are discussing the bankruptcy stay with debtor's counsel.

Don't let the nonbankruptcy defendants get the benefit of the bankruptcy stay by extending the stay beyond its scope. The bankruptcy stay only applies to the entity that actually filed for bankruptcy protection. See Bankruptcy Code Section 362(a)(1); *Seaboard Surety Co., v. Board of Freeholders*, 222 N.J. Super. 409 (App. Div. 1988). If a nondebtor defendant wants the benefits of the bankruptcy stay, it must either file a formal motion for a stay in the state court case (*Citizens First Nat. Bank v. Marcus*, 253 N.J. Super. 1 (App. Div. 1991), or file an adversary proceeding in the bankruptcy court under Bankruptcy Code Section 105 to obtain an injunction (see Fed.R.Bankr.P. 7001(7)).

Bankruptcy filings are up in volume and, depending on how the economy responds in 2010, may continue to be filed at a rapid rate. Personal injury lawyers must become familiar with the Bankruptcy Code and how it impacts their personal injury lawsuits. With a little help from local bankruptcy counsel, or some extended hours in the law library, personal injury lawyers can develop strategies to get them back to state court as soon as possible. However, lawyers who ignore the rules or battle trustees may find themselves before an unhappy bankruptcy judge on a fee application that is denied. ■