The Murky Intersection Between Bankruptcy Disclosure Requirements and an Individual's Fifth Amendment Right Against Self-Incrimination

by Elizabeth L. Gunn

Elizabeth L. Gunn is the bankruptcy specialist for the Commonwealth of Virginia Office of the Attorney General, Department of Social Services, Division of Child Support Enforcement.

The intersection of an individual's Fifth Amendment right to not be compelled to be a witness against himself and the Bankruptcy Code's inherent policy and requirements of full disclosure of all relevant information create a potential legal minefield for debtors and attorneys alike. While the Supreme Court has made it clear that the Fifth Amendment applies in civil bankruptcy proceedings, there is no guarantee that a debtor who appropriately invokes their privilege will be entitled to the full relief provided by the Bankruptcy Code. While Fifth Amendment rights will supersede the statutory plan for an efficient bankruptcy process, a debtor may not turn the shield of the Fifth Amendment into a sword to obtain a bankruptcy discharge without providing information sufficient for the provisions of the Bankruptcy Code to be carried out.

For parties and counsel, the two major issues that will arise when concerns related to the Fifth Amendment intersect with bankruptcy are: (1) was the privilege timely and appropriately invoked or was there waiver, including inadvertent waiver; and (2) if privilege was appropriately invoked, is there nevertheless sufficient information for the completion of the bankruptcy process and/or for the debtor to be entitled to a discharge.

The bankruptcy code requires a debtor, as part of the process of administration of the case, to prepare and file statements and schedules (§ 521), attend and testify at a meeting of creditors (§§ 341, 343), and turn over certain documents to a trustee or U.S. Trustee Program trustee. In addition, debtors in chapter 11 are required to prepare and file periodic operating reports (§ 1106(a)), and debtors in chapters 11, 12, and 13 are required to propose and confirm a plan of reorganization (e.g., § 1321). Each of these situations creates a potential hazard for the debtor in need of Fifth Amendment protections and a potential hurdle to the bankruptcy system's ability to effect a thorough and equitable adjudication of the process. In other words, in situations where a debtor is suspected of a crime, particularly a white-collar crime, or in which his records could help establish a criminal case against him, the full disclosure requirements of the Bankruptcy Code and Bankruptcy Rules may well be in direct conflict with his right and desire to keep silent.

Invoking Privilege

In order to invoke their Fifth Amendment privilege, bankruptcy debtors are treated like any other civil defendant. In particular, a bankruptcy debtor cannot make a total or blanket assertion of the privilege. Instead, the debtor must appear and be sworn as a witness, listen to the questions of the trustee or examining party, and specifically invoke the privilege to each question rather than answer. If there is a question as to the validity of the claim of privilege, the debtor may be required to show that they have reasonable cause to fear self-incrimination if the question is answered. In such a case, the Bankruptcy Court would have jurisdiction to hear and determine the claim of privilege.

However, the issue in bankruptcy many times is that the uninformed or careless debtor may have waived their privilege with respect to a portion or all of the questions or issues for which they are seeking protection. Waiver in a bankruptcy case can be inferred from a witness' course of conduct or prior statements concerning the subject of the case. Although waivers are not lightly inferred, where a debtor has prior testimony or disclosures that subsequent testimony would serve to flesh out, a waiver is likely to be found. For example, a debtor who completes statements and schedules and lists a debt to a secured creditor has likely waived any claim of privilege for questions related to the debt, the security interest, the note, payments, and any other contractual terms.

Courts have been extremely reluctant to allow an individual to rely on the privilege against self-incrimination as a shield after they have previously offered a one-sided version of the facts as a sword against the other side. Once the door is cracked, it will likely be opened completely and available to scrutiny on every exposed matter.

At this point it is important to note that the assertion of privilege (and therefore, the waiver thereof) is limited in bankruptcy to individuals and, just as in criminal cases, is not available to corporations or individuals acting as a corporate representative. In bankruptcy this distinction becomes especially important when individuals serve as officers, directors, or representative parties for a corporate entity. An individual cannot assert the privilege against self-incrimination when requested to turn over corporate documents or information in his possession, even if such documents may be incriminating to him personally. This distinction is limited to requests for information or documents in a representative capacity, if the individual is served or questioned in his individual capacity or even in his capacity as a former officer, director, or representative, then the privilege may still be properly invoked.

It is possible, especially in the case of parallel criminal and bankruptcy proceedings, that an individual may request and be granted immunity for her testimony. This proceeding is not governed by the bankruptcy court, but must go through the same process as any other federal grant of immunity—a request by an assistant U.S. attorney to the appropriate attorney general and approved by a U.S. district court. If a debtor requests immunity it is likely, though not required, that the bankruptcy court will continue all related bankruptcy proceedings until a determination is made as to the request. Notably, if immunity is granted, the debtor may no longer lawfully refuse to testify to the issues covered by the immunity or would risk losing their bankruptcy discharge (as discussed below). However, if immunity is not granted (or not offered), the debtor may refuse to testify, invoking his or her Fifth Amendment privilege.

Potential Consequences

As in other civil cases, the invocation of the privilege carries with it potential consequences. Similar to civil cases, the prevailing rule is that adverse inference(s) against parties may be made when they refuse to testify based upon a claim of privilege. The adverse inference has no per se evidentiary effect, but it may add to the weight of other evidence presented by a party to prove its case in chief.

The need for a debtor to provide significant information and documentation in order for the trustee or court to complete all necessary administrative bankruptcy actions results in additional consequences to the debtor who properly invokes privilege. Without a certain minimum level of disclosure by a debtor, proper administration of the case will likely be impossible and the debtor may face dismissal of their case. While at first blush dismissal may seem like a harsh result, with dismissal, the debtor's constitutional Fifth Amendment right and ability to obtain a discharge of his or her debts is preserved for a future date when the underlying privilege issues are no longer a concern. Alternatively, the debtor could face the more prejudicial denial of discharge. Bankruptcy Code § 727(b)(6) establishes the standards with respect to when a discharge can be denied in cases dealing with the claim of privilege and the grant, or failure to grant, immunity. In addition, the adverse inference of invoking the privilege can be used as part of a plaintiff's case in an action to deny discharge on any other basis provided for in the code.[1] In either case, the party seeking denial of discharge must make a prima facie evidentiary case apart from the proper invocation of the privilege; however, the adverse inference from the debtor's silence may be considered in denying a discharge. In certain circumstances, including denial of discharge for improper claim of privilege or failure to testify, any debts included in a case where a debtor is denied a discharge are specifically excepted from discharge in any future bankruptcy case, even if the debtor is granted a discharge in a subsequent case.[2]

Other potential consequences to a debtor who invokes the privilege include: (1) entry of a judgment declaring certain debt(s) are nondischargeable based upon the evidence combined with the adverse inference of invoking the privilege[3]; (2) denial of confirmation of a chapter 11, 12, or 13 plan of reorganization for a lack of sufficient evidence on behalf of the debtor to meet the confirmation requirements, particularly the element that the plan be proposed in good faith; (3) striking of evidence presented by a debtor who later invokes the privilege when cross-examined on the same; or (4) other civil penalties.

A debtor may seek to stay his or her bankruptcy case pending the resolution of the potential criminal matter, but such stay requires the debtor to meet the elements for a preliminary injunction and are generally considered an extremely high burden. However, most bankruptcy judges may be willing to exercise inherent power to manage their docket in such a way to provide some limited period of time for resolution.

Conclusion

Debtors in bankruptcy who are hesitant to make a full and complete disclosure of their debts, assets, and financial situation and answer questions thereon, may face many difficult and tricky choices. In addition, uninformed or inattentive decisions or disclosures during the inception of the case and continuing throughout the administration of the case could have serious consequences, including the loss of the protection afforded by the Fifth Amendment against self-incrimination. Criminal attorneys with clients considering bankruptcy and bankruptcy attorneys whose clients may have criminal concerns must be aware of, advise their clients about, and pay acute attention to those areas where the elements of invocation of an individual's Fifth Amendment privilege intersect with the disclosure requirements of bankruptcy.[4] ⊙

Endnotes

[1]Grounds for denial of discharge under most chapters can be found in 11 U.S.C. § 727(a).

[2]11 U.S.C. § 523(a)(10).

[3]Grounds for determination of nondischargeability of a debt can be found in 11 U.S.C. § 523.

[4]For more detailed analysis of each of the topics discussed herein, the author highly recommends the following: Timothy R. Tarvin, *The Privilege Against Self-Incrimination in Bankruptcy and the Plight of the Debtor*, 44 Seton Hall L. Rev. 47 (2014); and Craig Peyton Gaumer & Charles L. Nail Jr., *Truth or Consequences: The Dilemma of Asserting the Fifth Amendment Privilege Against Self-Incrimination in Bankruptcy Proceedings*, 76 Neb. L. Rev. 497 (1997).