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## Getting Personal: Acquiring PII Out of Bankruptcy

Salesforce, a software company specializing in customer-relationship-management programs, generated \$21.25 billion in revenue in 2021.<sup>1</sup> On its website, Salesforce plays amateur anthropologist, noting that “[e]ven in Palaeolithic times, there must have been an understanding that it is easier to sell to an existing customer than find a new one, and that it was advantageous to nurture the relationship. We are not sure how this information was stored, whether it was simply committed to memory (where competitors could not access it), or whether some early customer list was maintained.”<sup>2</sup>

Regardless of Salesforce’s historical claims, customer data is clearly of significant value to a company’s bottom line. Facebook, Google and other technology companies have generated numerous headlines regarding the volume of data collected on their customers and the profitable uses of that data.<sup>3</sup> The value of this asset is not unique to financially healthy organizations; for companies in bankruptcy, consumer data can also prove extremely valuable. Debtors and trustees, as fiduciaries, must carefully consider how best to maximize the value of any consumer data in the estate.

However, federal, state and international laws restrict a debtor’s use of consumer data, including sometimes-stringent restrictions on its sale.<sup>4</sup> Such laws are most concerned with protecting personally identifiable information (PII), or information that may be linked to a specific person. In addition to the restrictions on the use of PII imposed by non-bankruptcy laws, the Bankruptcy Code mandates the protection of PII by requiring that any sale of PII comply with the debtor’s existing privacy policy, and if the sale violates that policy, it requires the appointment of a consumer privacy ombudsperson (CPO) to advise on that sale.

These considerations become particularly salient in retail bankruptcy cases, where consumer data such as customer profiles are an important asset. Cleansed and sold properly, consumer data may be

critical to the successful continuation of a business line or a meaningful distribution to estate creditors.

This article discusses the history and current state of regulation regarding the sale of PII in bankruptcy and provides some general guidance concerning monetization of this asset. While this article focuses on the prospective upside of consumer data, such data may also present a liability if it was collected, used or stored unlawfully, and both the estate and potential buyers should be careful in assessing the pitfalls of selling or acquiring such data.<sup>5</sup>

### What Is PII in Bankruptcy?

Whatever a debtor owns once its bankruptcy petition is filed constitutes property of the debtor’s estate.<sup>6</sup> However, “[p]roperty interests are created and defined by state law.”<sup>7</sup> A state’s restrictions on the transferability of an asset generally “limits the ownership interest in the property” by removing the unfettered right to transfer.<sup>8</sup> Likewise, a contractual restriction, such as the terms of a privacy policy, might restrict the transferability of PII in bankruptcy.

It is well settled that PII is property of the estate.<sup>9</sup> The Bankruptcy Code defines PII as the “names, mailing addresses, email addresses, phone numbers, Social Security numbers, and credit card account numbers that are provided by an individual to a debtor in connection with obtaining products or services primarily for personal, family or household purposes.”<sup>10</sup> A typical business bankruptcy case, particularly in the retail context, may present a staggering volume of valuable PII.<sup>11</sup> However, if the information was either aggregated in violation of nonbankruptcy law or cannot be legally sold or assigned, even the most data-rich customer profiles may prove worthless due to concrete transfer restrictions.<sup>12</sup>



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1 Salesforce’s revenue can be found on the *Fortune 500* list, available at [fortune.com/fortune500](https://fortune.com/fortune500) (unless otherwise specified, all links in this article were last visited on March 22, 2022).

2 See “The Complete History of CRM,” Salesforce, available at [salesforce.com/ap/hub/crm/the-complete-crm-history](https://salesforce.com/ap/hub/crm/the-complete-crm-history).

3 See, e.g., Sheila Dang & Nivedita Balu, “Facebook Ad Revenue Seen Feeling Brunt of Apple’s Privacy Changes,” Reuters (Oct. 25, 2021), available at [reuters.com/technology/facebook-ad-revenue-seen-feeling-brunt-apple-privacy-changes-2021-10-25](https://reuters.com/technology/facebook-ad-revenue-seen-feeling-brunt-apple-privacy-changes-2021-10-25) (subscription required to view article).

4 Personal health information is governed by separate Code provisions and under laws such as the Health Insurance Portability and Accountability Act of 1996, and is outside the scope of this article.

5 See, e.g., Donna M. Airoldi, “Marriott Fined Nearly \$24 Million for Starwood Data Breach,” *Bus. Travel News* (Oct. 30, 2020), available at [businesstravelnews.com/Lodging/Marriott-Fined-Nearly-24M-for-Starwood-Data-Breach](https://businesstravelnews.com/Lodging/Marriott-Fined-Nearly-24M-for-Starwood-Data-Breach) (noting fine to Marriott for data breach that occurred at Starwood prior to Marriott’s acquisition).

6 11 U.S.C. § 541(a), with certain statutory exceptions enumerated in 11 U.S.C. § 541(b).

7 *Butner v. United States*, 440 U.S. 48, 55, 99 S. Ct. 914, 918, 59 L. Ed. 2d 136 (1979).

8 *In re C-Power Prod. Inc.*, 230 B.R. 800, 803 (Bankr. N.D. Tex. 1998) (finding that malpractice claim arising under Texas law could not be assigned under 11 U.S.C. § 363).

9 See *Debrececi v. Bru-Jell Leasing Corp.*, 710 F. Supp. 15, 21 (D. Mass. 1989) (“Property is broadly defined in the [C]ode, see 11 U.S.C. § 541, and includes intangibles such as customer lists and goodwill.”).

10 11 U.S.C. § 101(41A).

11 “From Addresses to Purchase Histories, Customer Data Is Driving Retail Bankruptcy Acquisitions,” *Fashion Law* (Aug. 20, 2020), available at [thefashionlaw.com/bankruptcy-bidders-wants-customer-data-and-ailing-retailers-are-selling](https://thefashionlaw.com/bankruptcy-bidders-wants-customer-data-and-ailing-retailers-are-selling).

12 See, e.g., *In re Toysmart.com LLC*, Case No. 00-13995-CJK (Bankr. E.D. Mass. July 20, 2000).

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## PII in Bankruptcy: Where We've Been

### Toysmart

Restrictions on the sale of PII in bankruptcy are less than three decades old. In 2000, *In re Toysmart.com LLC*<sup>13</sup> first raised the issue of a debtor violating its own privacy policy by attempting to sell PII in the course of a § 363 auction. In 1999, online toy store Toysmart adopted a privacy policy that promised that it would never sell or share customer data with third parties. However, by 2000 Toysmart, then in the midst of its chapter 11 case, sought to conduct a public auction of its assets, including its customer data.<sup>14</sup>

In response, the Federal Trade Commission (FTC) sued Toysmart to enjoin the proposed auction, alleging that the proposed sale violated the FTC Act as an unfair and deceptive trade practice by violating the debtor's privacy policy.<sup>15</sup> To settle the lawsuit, Toysmart agreed to limit its potential buyers to only a similarly situated buyer, which agreed to abide by Toysmart's privacy policy.<sup>16</sup> Toysmart was unable to find a buyer with such restrictions and pulled the PII from the auction, and Disney Corp., one of Toysmart's investors, ultimately paid to have the data destroyed.<sup>17</sup>

### BAPCPA and the CPO

In 2005, the Bankruptcy Abuse Prevention and Consumer Protection Act (BAPCPA) amendments changed how sales of PII were treated under the Bankruptcy Code. BAPCPA added the Code's current definition of PII, imposing new restrictions on the sale of PII and creating the position of CPO.

Section 363(b)(1) was amended to prevent a debtor from selling or leasing PII outside the ordinary course of business unless either (1) the sale or lease does not violate the debtor's privacy policy in effect on the petition date, or (2) a CPO is appointed under § 332 of the Code and the court approves the sale after finding that the sale does not violate applicable nonbankruptcy law.<sup>18</sup>

If a debtor wants to sell PII in violation of its privacy policy, the bankruptcy court must order the U.S. Trustee to appoint a CPO no later than seven days before the sale.<sup>19</sup> The CPO investigates the debtor's privacy policy and its data, then provides the court with information relating to the debtor's privacy policy, the potential losses or gains of privacy and potential costs or benefits to consumers if the court approves the sale, and alternatives that would mitigate potential privacy losses or potential costs to consumers.<sup>20</sup>

If the *Toysmart* case occurred today, § 363(b)(1) would mandate a CPO's appointment to advise on the proposed sale that violates the debtor's privacy policy. The CPO would assess the potential sale, the debtor's privacy policy and the debtor's data, then likely recommend that the bankruptcy court impose conditions on the sale. Common conditions imposed are to require the buyer to be in the same line of business as the debtor and agree to some or all of the following: (1) use PII for the same purpose as specified in the debtor's privacy policy; (2) comply with the debtor's privacy policy; (3) notify all consumers and provide a right to opt out of changes to those policies or to new uses of their PII before making material changes to the privacy policy or using or disclosing PII in a different manner from that specified in the debtor's privacy policy; (4) employ appropriate information security controls to protect PII; and (5) abide by any applicable state privacy and data-breach laws.<sup>21</sup> By suggesting such conditions, a CPO often provides the bankruptcy court with information to allow a noncompliant sale to proceed while minimizing harm to the affected consumers.

**Compared to the relatively strong consumer protections available within bankruptcy, the protections afforded to consumers in data sales outside of bankruptcy vary widely.**

### RadioShack

In 2015, *In re RadioShack*<sup>22</sup> provided a highly publicized example of how a debtor may sell PII in violation of its privacy policy by agreeing to drastically limit the data sold and to impose restrictions on the buyer. The debtor in *RadioShack* proposed to sell 117 million customer records in a § 363 sale. After the FTC<sup>23</sup> and the attorneys' general of 38 states<sup>24</sup> objected to the sale as violating state law and the company's privacy policy, the parties reached a settlement with the participation of the CPO. The settlement<sup>25</sup> drastically narrowed the scope of customer data sold to the buyer by restricting both the age and categories of data sold.

All of the transferred PII remained subject to RadioShack's privacy policy, and all other data not trans-

<sup>13</sup> *Id.*

<sup>14</sup> Andrew B. Buxbaum & Louis A. Curcio, "When You Can't Sell to Your Customers, Try Selling Your Customers (but Not Under the Bankruptcy Code)," 8 *ABI L. Rev.* 395, 399 (Winter 2000), available at [abi.org/members/member-resources/law-review](http://abi.org/members/member-resources/law-review).

<sup>15</sup> See "FTC Announces Settlement with Bankrupt Website Toysmart.com Regarding Alleged Privacy Policy Violations," FTC Press Release (July 21, 2000), available at [ftc.gov/news-events/news/press-releases/2000/07/ftc-announces-settlement-bankrupt-website-toysmartcom-regarding-alleged-privacy-policy-violations](http://ftc.gov/news-events/news/press-releases/2000/07/ftc-announces-settlement-bankrupt-website-toysmartcom-regarding-alleged-privacy-policy-violations).

<sup>16</sup> *Id.*

<sup>17</sup> See Linda Rosencrance, "Disney Expected to Pay Toysmart.com to Destroy Customer List," *Computer World* (Jan. 9, 2001), available at [computerworld.com/article/2590344/disney-expected-to-pay-toysmart-com-to-destroy-customer-list.html](http://computerworld.com/article/2590344/disney-expected-to-pay-toysmart-com-to-destroy-customer-list.html).

<sup>18</sup> 11 U.S.C. § 363(b)(1).

<sup>19</sup> *Id.*

<sup>20</sup> *Id.*

<sup>21</sup> These conditions were first outlined in *In re Storehouse Inc.*, No. 06-11144 (Bankr. E.D. Va. Sept. 11, 2007).

<sup>22</sup> See Notice of Agreement Regarding Sale of Certain Personally Identifiable Information, *In re RadioShack Corp.*, Case No. 15-10197 (BLS) (Bankr. D. Del. May 20, 2015).

<sup>23</sup> "FTC Requests Bankruptcy Court Take Steps to Protect RadioShack Consumers' Personal Information," FTC Press Release (May 18, 2015), available at [ftc.gov/news-events/news/press-releases/2015/05/ftc-requests-bankruptcy-court-take-steps-protect-radioshack-consumers-personal-information](http://ftc.gov/news-events/news/press-releases/2015/05/ftc-requests-bankruptcy-court-take-steps-protect-radioshack-consumers-personal-information).

<sup>24</sup> See "Attorney General Paxton Announces Agreement to Protect Consumer Privacy in RadioShack Case," Texas Attorney General Press Release (May 20, 2015), available at [texasattorneygeneral.gov/news/releases/attorney-general-paxton-announces-agreement-protect-consumer-privacy-radioshack-case](http://texasattorneygeneral.gov/news/releases/attorney-general-paxton-announces-agreement-protect-consumer-privacy-radioshack-case).

<sup>25</sup> See Notice of Agreement Regarding Sale of Certain Personally Identifiable Information, *In re RadioShack Corp.*, Case No. 15-10197 (BLS) (Bankr. D. Del. May 20, 2015).

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ferred was destroyed. Further, the buyer agreed to provide notice and opt-out opportunities to persons whose PII was transferred.<sup>26</sup> The settlement generated considerable press, both from the attorneys' general touting their success in protecting consumers, and from the public in reaction to a large company trying to sell the information of so many of its customers.<sup>27</sup>

## Where We Are Now, and Where We're Going

As time passes, there are fewer debtors without privacy policies permitting the sale of consumer data in a bankruptcy, as such clauses are standard in most current privacy policies. In the absence of a debtor's privacy policy in effect on the petition date prohibiting such a sale, the Code's plain language does not mandate the CPO's appointment.<sup>28</sup> However, the sale of PII may still draw an objection from a third party (government or private). Voluntarily narrowing the scope of data sold and seeking purchasers in the same line of business may stave off such objections and assuage concerns from the bankruptcy court.

The scope of privacy laws increases each year. At the time that BAPCPA was passed, no U.S. state had a comprehensive consumer data privacy law. As of this spring, five states have passed either consumer-data privacy laws or laws restricting the sale of PII,<sup>29</sup> with bills introduced in another 20 states.<sup>30</sup> While most of these laws have at least some carve-outs for the sale of PII in a bankruptcy or merger,<sup>31</sup> they also impose additional requirements for the treatment of PII that debtors and potential purchasers must follow to avoid sale objections. There is also the specter of federal consumer data privacy legislation similar to the European

Union's General Data Protection Regulation or California's Consumer Protection Act.

## Purchasing PII from Insolvent or Distressed Companies

Compared to the relatively strong consumer protections available within bankruptcy, the protections afforded to consumers in data sales outside of bankruptcy vary widely. In the absence of a state law or an industry-specific regulation, consumers' only significant recourse is the company's privacy policy, which likely permits the sale of PII in a merger or acquisition. If a company chooses to sell PII in violation of its promises, consumers will also likely have to rely on either some type of class action litigation, the FTC or state attorneys general for enforcement and protection.

While not subject to as much oversight as a company in bankruptcy, a distressed company seeking to sell PII should still carefully evaluate its current and past privacy policies and make appropriate revisions with ample time prior to selling the data to a third party in violation of its policies. If a company wishes to revise its policy to permit such a sale or transfer, it should provide customers with notice and at least a 30-day period to obtain affirmative consent, since the privacy policy is materially changing from a prior version.<sup>32</sup> These actions will dramatically reduce the threat of government enforcement actions or consumer-related litigation. By taking such steps (and by seeking legal advice), a business can ensure that it is complying with relevant law and that the data it wishes to sell remains valuable.

## Conclusion

To retain its considerable value, the collection and transfer of PII must be handled properly. If not, both the distressed company and its potential purchaser may be saddled with worthless data or with additional liability. **abi**

<sup>26</sup> See Texas Attorney General Press Release, *supra* n.24.

<sup>27</sup> See, e.g., Michael Hiltzik, "The RadioShack Bankruptcy Shows You Can't Trust a Company's Privacy Pledge," *Los Angeles Times* (May 19, 2015), available at [latimes.com/business/la-fi-mh-radioshack-you-have-no-privacy-left-20150519-column.html](http://latimes.com/business/la-fi-mh-radioshack-you-have-no-privacy-left-20150519-column.html).

<sup>28</sup> See, e.g., *In re Lucky Brand Dungarees LLC*, No. 20-11768 (CSS), 2020 WL 4698654 (Bankr. D. Del. Aug. 12, 2020) at \*4 (noting that debtor's privacy policy permitted bankruptcy sale and therefore no CPO was required).

<sup>29</sup> California, Colorado, Virginia and Utah have passed consumer data privacy laws. In 2019, Nevada passed a law requiring businesses to provide consumers the right to opt out of the sale of their PII.

<sup>30</sup> See "U.S. State Privacy Legislation Tracker," Int'l Ass'n of Privacy Prof'ls, available at [iapp.org/resources/article/us-state-privacy-legislation-tracker](http://iapp.org/resources/article/us-state-privacy-legislation-tracker).

<sup>31</sup> See Cal. Civ. Code § 1798.140(ad)(1); Colo. Rev. Stat. Ann. § 6-1-1303(23)(b)(IV) (effective July 1, 2023); Va. Code Ann. § 59.1-583 (effective Jan. 1, 2023).

<sup>32</sup> The FTC requires notice to consumers prior to a material change in a privacy policy. See, e.g., "Letter from Jessica L. Rich, Director of the Federal Trade Commission Bureau of Consumer Protection," Fed. Trade Comm'n (April 10, 2014), available at [ftc.gov/system/files/documents/public\\_statements/297701/140410facebookwhatapptr.pdf](http://ftc.gov/system/files/documents/public_statements/297701/140410facebookwhatapptr.pdf).

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