

IN THE UNITED STATES BANKRUPTCY COURT FOR THE NORTHERN DISTRICT OF
IOWA

IN RE:)

) Chapter 7

LOREN REISEN)

PATRICIA REISEN) Bankruptcy No. 03-01999

)

Debtors.)

ORDER RE MOTION FOR SANCTIONS

On January 22, 2004, the above-captioned matter came on for hearing pursuant to assignment on a Motion for Sanctions filed by Debtor. Debtor Patricia Reisen appeared in person with Attorney Paul Fitzsimmons. Diane Troester, head of the cash office for Wal-Mart in Dubuque, Iowa appeared for Wal-Mart without counsel. The Dubuque County Attorney's Bad Check Restitution Program did not appear at any time during these proceedings. On January 20, 2004, however, Kristine Bradshaw, Regional Manager for American Corrective Counseling Services, faxed a signed affidavit to the Court entitled "Statement of Facts". Also present at the hearing, though not a party, was Dubuque County Attorney Fred McCaw. This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(O).

STATEMENT OF THE CASE

Loren and Patricia Reisen filed their Chapter 7 petition for bankruptcy May 21, 2003. Wal-Mart is listed as a creditor in the schedules. The amount of the debt is listed as \$111.71. It is generally acknowledged that this debt arose because of an insufficient funds check written by Debtor Patricia Reisen to Wal-Mart in Dubuque, Iowa on March 24, 2003. Postpetition, Wal-Mart turned the check over to the Dubuque County Attorney's Bad Check Restitution Program which sent a demand letter to Debtor on August 14, 2003. After receiving this letter, Debtor filed a Motion for Sanctions asserting that Wal-Mart and the Dubuque County Attorney's Bad Check Restitution Program violated 11 U.S.C. § 362.

FINDINGS OF FACT

The record in this case is unorthodox. The matter was initially scheduled for hearing in Dubuque in December 2003. It was reset to provide notice of the pendency of this action to the Dubuque County Attorney's Office, which is peripherally involved in these allegations. The original Motion for Sanctions was served on the Dubuque, Iowa Wal-Mart Store and the Dubuque County Attorney's Bad Check Restitution Program ("Restitution Program"). No responsive pleadings were filed prior to the present hearing.

Debtor Patricia Reisen was present at the hearing. The Dubuque County Attorney, Fred McCaw, attended the hearing and explained the Restitution Program's operations. American Corrective Counseling Services, Inc. (ACCS) serves as the Restitution Program's manager. ACCS did not appear at the hearing, but filed an affidavit from Kristine Bradshaw, ACCS' Regional Manager. The Dubuque County Attorney's Bad Check Restitution Program, which communicated with Debtor,

is part of a nationwide program run by the American Corrective Counseling Services. Any sanctions imposed for the Dubuque County Attorney's Bad Check Restitution Program's actions are the legal responsibility of American Corrective Counseling Services. Wal-Mart's counsel did not attend the hearing, but Ms. Diane Troester, head of the local Wal-Mart's cash office, was present.

The factual record is not in serious dispute. Debtor Patricia Reisen wrote an insufficient funds check to the Dubuque, Iowa Wal-Mart Store in the amount of \$111.71 on March 24, 2003. In May 2003, Wal-Mart sent a letter to Debtor indicating that Wal-Mart was holding the insufficient funds check. This contact was pre-petition and appropriate. Debtor did not take any corrective action.

Debtors filed a joint Chapter 7 petition on May 21, 2003. Wal-Mart received notice of the pendency of the bankruptcy. Ms. Troester testified that she handles all bankruptcy matters and that Wal-Mart's policy is to terminate all contact with the Debtor upon notification of bankruptcy. Ms. Troester showed the Court a register of bankruptcy filings and bad checks written to Wal-Mart. The system for dealing with both is well-organized and clearly documented.

Ms. Troester testified that she turned Debtor's check over to the County Attorney's Office and that she filed Wal-Mart's complaint with the Restitution Program on August 13, 2003. Wal-Mart took no further action against Debtor. Wal-Mart's reason for continuing to process Debtor's insufficient funds check post-petition is the crucial fact in the case against Wal-Mart.

Ms. Troester testified that after Debtor filed this Motion for Sanctions, she examined her records individually and discovered that she had inadvertently stapled the notice of Debtor's bankruptcy underneath another individual's paperwork. The Court observed Ms. Troester's testimony and concludes that her testimony was candid and truthful.

According to County Attorney McCaw, the County Attorney's Restitution Program is an independent contractor. It attempts to collect on bad checks for the County, receiving a percent of collections as compensation. This is apparently a nationwide program. The administrator of the program is the American Corrective Counseling Services Inc., headquartered in San Clemente, California. The Restitution Program evaluated Wal-Mart's complaint according to the County Attorney's eligibility requirements. The Restitution Program sent Debtor a demand letter on August 14, 2003. It is this letter which forms the basis of Debtor's motion against the Restitution Program. The ACCS affidavit states that the demand letter was part of the ordinary processing of an insufficient funds check complaint. At this point, the Restitution Program had no notice of Debtor's pending bankruptcy.

Debtor Patricia Reisen telephoned the Restitution Program on August 18, 2003, after receiving the August 14 demand letter. According to the ACCS affidavit, Mrs. Reisen stated that she was going to contact her bankruptcy attorney. Debtor's attorney, Mr. Fitzsimmons, wrote a letter to the Restitution Program advising them of the pendency of the bankruptcy on August 18, 2003. Mr. Fitzsimmons received a written response from the Dubuque County Attorney's Office on September 25, 2003.

Debtor received her discharge order on September 4, 2003.

The underlying debt to Wal-Mart was listed on Debtor's bankruptcy schedules. Wal-Mart did not challenge discharge of this debt. The Certificate of Mailing the discharge order was dated September 6, 2003. Mr. Fitzsimmons sent a second letter to the Dubuque County Attorney's Office on September 26, 2003, explaining the automatic stay and the alleged violations.

After Debtor's Motion for Sanctions was filed on September 30, 2003, a Restitution Program representative spoke to Ms.

Troester from Wal-Mart. According to the ACCS affidavit, only

then did the Restitution Program learn of Debtor's pending bankruptcy despite the two previous contacts from Mr.

Fitzsimmons.

After receiving Mr. Fitzsimmon's August 18 letter, notice of Debtor's Motion for Sanctions, and speaking to Ms.

Troester, the Restitution Program sent out four additional notices. The first is captioned "Official Notice" and dated October 13, 2003. Although the letter was addressed to Patricia Reisen, the Restitution Program mailed the letter to Mr. Fitzsimmon's office address. This notice states that there is a cash balance due of \$271.71. It also warns Debtor that failure to contact the Restitution Program could result in criminal prosecution.

On November 24, 2003, the Restitution Program sent Debtor a second notice at Mr. Fitzsimmon's address. This one is entitled "Warning" and threatened Debtor with "potential arrest and prosecution" if she did not contact the Restitution Program immediately.

The Restitution Program sent a "Final Notice" to Debtor, again through her attorney, on December 9, 2003. It states the following:

Due to your failure to complete the requirements of the County Attorney's Bad Check Restitution Program as specified in previous notices, we are now initiating steps toward formal prosecution proceedings against you. Criminal charges for Theft by a Worthless Check are being prepared for review by an Assistant County Attorney.

If you desire to halt this action, or if you believe there has been an error, contact this office at (888)613-6398 within 24 hours upon receipt of this notice.

The final contact from the Restitution Program, dated January 8, 2004 and again addressed to Patricia Reisen at her attorney's address, is captioned "Important Notice." This notice asks Ms. Reisen to contact the Restitution Program immediately "regarding a bad check crime report on file." All four notices are signed by Mrs. Miller, Case Coordinator for the Restitution Program.

CONCLUSIONS OF LAW

Section 362 imposes the automatic stay when the debtor files a bankruptcy petition. 11 U.S.C. § 362; In re Knaus, 889 F.2d 773, 774 (8th Cir. 1989); In re Goodfellow, 298 B.R. 358, 361 (Bankr. N.D. Iowa 2003). The stay is extremely broad, and prevents any attempt to collect pre-petition debts.

11 U.S.C. § 362; Knaus, 889 F.2d at 774; Goodfellow, 298 B.R. at 361. Debtor must demonstrate by a preponderance of the evidence that Defendants violated the automatic stay. See, e.g., In re Estep, 173 B.R. 126, 129 (Bankr. N.D. Ohio 1994) (citing Grogan v. Garner, 498 U.S. 279, 286 (1991)); In re Bandy, No. 03-00753,

2003 WL 21781995, at *2 (Bankr. N.D. Iowa July 29, 2003). Defendants have the burden of proof regarding any defenses, including the applicability of any § 362 (b) exceptions to the stay. In re Westman, 300 B.R. 338, 342 (Bankr. D. Minn. 2003).

The automatic stay was imposed when Debtor filed for Chapter 7 relief on May 21, 2003. Wal-Mart admits to sending Debtor's insufficient funds check to the Restitution Program on August 13, 2003. This violated the automatic stay, unless a § 362(b) exception applies to Wal-Mart's actions.

Exceptions to the Automatic Stay

Section 362(b)(1) excepts the commencement of criminal proceedings from the automatic stay. 11 U.S.C. § 362(b)(1). In general, exceptions to the automatic stay are interpreted narrowly. See, e.g., In re National Cattle Congress, Inc., 179 B.R. 588, 595 (Bankr. N.D. Iowa 1995) ("[T]he § 362(b) exceptions are intended to be read narrowly."); In re Claussen, 118 B.R. 1009, 1017 (Bankr. D. S.D. 1990). Although this Court has not addressed the issue, other courts have and are split as to whether (b)(1) excepts all criminal prosecutions, regardless of the creditor's motive for filing its criminal complaint, or only those criminal prosecutions that a creditor initiates for a purpose other than the collection of a pre-petition debt.

One line of cases excepts all criminal prosecutions against the debtor regardless of the purpose in filing. See In re Bibbs, 282 B.R. 876, 880 (Bankr. E.D. Ark. 2002) ("[T]he automatic stay does not apply to criminal prosecutions. Period. . . . On its face, it does not provide any exception for prosecutorial purposes or bad faith."); In re Hartung, 258 B.R. 210, 214 (Bankr. D. Mont. 2000) (finding automatic stay does not prevent creditor from reporting a crime as every citizen has a duty to report criminal activity). Under this view, Wal-Mart's action would not violate the stay.

The alternative line of cases follows the "principal motivation" test. Courts applying this test scrutinize the main purpose behind the criminal prosecution. If the main purpose is debt collection, not the greater public good, then the criminal prosecution violates the stay. See, e.g., In re DeLay, 48 B.R. 282, 286 (Bankr. W.D. Mo. 1984) ("Maintenance of a criminal prosecution against a debtor violates letter and spirit of bankruptcy laws only if its principal purpose is to collect a dischargeable debt."); In re Butler, 74 B.R. 106 (Bankr. W.D. Mo. 1985); In re Wagner, 18 B.R. 339 (Bankr. W.D. Mo. 1982).

Under this test, the central issue for the court to determine is whether the creditor's actions were "designed to collect a claim from the debtor." DeLay, 48 B.R. at 286 (emphasis in original). Courts resolve this question on a case-by-case, fact sensitive basis. It is the conclusion of this Court that the principal motivation test provides the most balanced approach to accommodating the prosecutorial functions as well as protecting the rights of debtors. This test will be applied here.

Section 362(b)(4) excepts proceedings by a governmental unit to enforce its police or regulatory power. 11 U.S.C. § 362(b)(4). In order for the (b)(4) exception to apply, (1) the party initiating the action must be a governmental unit; and (2) the proceedings must be for a police or regulatory purpose. 11 U.S.C. § 362(b)(4); See In re Commonwealth Cos., 913 F.2d 518, 521-22 (8th Cir. 1990); Illinois v.

Elec. Utilities, 41 B.R. 874 (Bankr. N.D. Ill. 1984). Under 11 U.S.C. § 101(27), a "governmental unit" includes a "department, agency, or instrumentality of the United States . . . a State, a Commonwealth, a District, a Territory, a municipality, or a foreign state." 11 U.S.C. § 101(27).

Case law analyzing what constitutes an "instrumentality" has concentrated on state bar, labor law enforcement, rent regulation, minimum wage, and environmental violations proceedings. 1 Collier Bankruptcy Manual § 362.05[4][a][I] (Lawrence P. King, ed., Matthew Bender 3d ed. 2003). In determining whether these entities are "instrumentalities" under § 101(27), most courts have focused on (1) the degree of control the governmental unit exercises over the instrumentality; and (2) whether the instrumentality's functions are normally associated with the government. See, e.g., In re Wade, 948 F.2d 1122 (9th Cir. 1991) (finding the State Bar of Arizona is an "instrumentality" based upon the degree of control the Arizona Supreme Court exercises over the Bar); In re Williams, 158 B.R. 488 (Bankr. D. Idaho 1993) (finding the Idaho State Bar an "instrumentality" based upon both the Idaho Supreme Court's control over the Bar and the Bar's performance of governmental functions).

The Restitution Program, under this analysis, is not an instrumentality of the Dubuque County Attorney. The Restitution Program is a collection agency associated with the Dubuque County Attorney's Office as an independent contractor. It was not created by the Dubuque County Attorney's Office. Cf. Wade, 948 F.3d at 1124 (emphasizing that Arizona State Bar exists due to Arizona Supreme Court rule authorizing it to regulate lawyers in Arizona). If an insufficient funds check complaint meets the criteria specified by the County Attorney's Office, then the complaint is referred to the Restitution Program. The County Attorney has no further control over the Restitution Program's actions unless the Restitution Program's attempts at debt collection fail. Cf. id. ("Although the State Bar plays a part in the enforcement of the rules, its role is completely defined by the court; the [State Bar] acts as the agent of the court under its continuous supervision.").

The Restitution Program exists to facilitate the payment of bad checks. It operates under typical debt collection rules. While the State certainly has an interest in ensuring that checks are paid, the Restitution Program's function is more similar to private debt collection than a typical government function. Cf. Williams, 158 B.R. 490 (State Bar regulates and disciplines lawyers, "functions normally associated with the government.").

Sanctions for Violation of the Automatic Stay

Section 362(h) sets forth the remedy for a willful violation of the automatic stay:

(h) An individual injured by any willful violation of a stay provided by this section shall recover actual damages, including costs and attorneys' fees, and, in appropriate circumstances, may recover punitive damages.

To recover the damages set forth in § 362(h), the violation must be "willful." 11 U.S.C. § 362(h). There is a "willful" violation of the automatic stay when "the creditor acts deliberately with knowledge of the bankruptcy

petition." Knaus, 889 F.2d at 775; In re Dencklau, 158 B.R. 796, 799 (Bankr. N.D. Iowa 1993).

In determining actual damages, the "court has discretion to fashion the punishment to fit the circumstances." In re Joens, No. 03-02077, 2003 WL 22839822, at *3 (Bankr. N.D. Iowa Nov. 21, 2003); In re Adams, No. 01-9226, 2002 WL 844350, at *4 (Bankr. N.D. Iowa Apr. 19, 2002) ("[I]t is the conclusion of this Court that a mechanical application of these [automatic stay] rules is inappropriate. The rules must be considered in the context of the case."). Costs and attorneys' fees are available, but only if there is also sufficient evidence for a finding of actual damages. Joens, 2003 WL 22839822, at *3. The court may award punitive damages under § 362(h) only where the action taken is "egregious, intentional misconduct on the violator's part." In re Ketelson, 880 F.2d 990, 993 (8th Cir. 1989); Dencklau, 158 B.R. at 801.

Ms. Troester testified that she turned over the insufficient funds check due to an inadvertent filing error. She stated that Wal-Mart's policy is to terminate all actions to collect insufficient funds checks against those who file for bankruptcy. Wal-Mart's actions do technically violate the automatic stay. Wal-Mart had notice of Debtor's bankruptcy and deliberately sent the insufficient funds check to the Restitution Program. Ms. Troester's testimony established, however, that Wal-Mart's action was due to a simple filing error. The violation was technical. Courts have been unwilling to impose sanctions if the violation is technical or harmless. Adams, 2002 WL 844350, at *3; In re Oxford Dev., 115 B.R. 216, 218 (Bankr. W.D. Mo. 1990) (denying sanctions for technical violation of automatic stay).

The Restitution Program's initial demand letter, dated August 14, 2003, was not willful. The Restitution Program was not a listed creditor, thus it received no initial notice of Debtor's bankruptcy petition. Wal-Mart did not notify the Restitution Program of Debtor's bankruptcy due to the filing error.

SUMMARY

Debtors filed their Chapter 7 petition on May 21, 2003 and their discharge order was entered on September 4, 2003. Debtor have brought this motion against Wal-Mart and the American Corrective Counseling Services for violations of the automatic stay under § 362. For the reasons set out herein, the Court finds that the only act done by Wal-Mart during the pendency of the automatic stay was to send the insufficient check to the Restitution Program. However, for the reasons set forth in this opinion, the Court determines that this was an accidental violation and technical in nature. The Court concludes that Wal-Mart committed no willful act during the pendency of the automatic stay sufficient to impose sanctions. Wal-Mart had no contact with Debtor after the entry of discharge on September 4, 2003.

This Court also concludes that, although the Restitution Program sent a demand letter to Debtor on August 14, 2003, the same was not willful because the Restitution Program had never received notification of Debtors' pending bankruptcy. After the Restitution Program was notified by Debtor and her counsel of the pendency of the bankruptcy and the automatic stay, no further contact was made by the Restitution Program during the period when the automatic stay remained in effect until the entry of the discharge on September 4, 2003.

Therefore, it is also the conclusion of the Court that the Restitution program did not commit any act during the pendency of the automatic stay which would warrant the imposition of sanctions.

DISCHARGE INJUNCTION

Ordinarily, the foregoing would complete the analysis and Debtor's Motion for Sanctions would be denied. However, the Court must comment about certain additional facts which prevent this case from being completely resolved. The discharge was entered on September 4, 2003 at which point the discharge injunction under § 524 replaces the automatic stay under § 362. The Court previously stated that the Restitution Program had no contacts after August 14, 2003 with Debtor until the entry of the discharge on September 4, 2003. Although this is correct, it does not address the period of time after the September 4, 2003 discharge until the time of

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the hearing in this case in January, 2004. It is beyond dispute that, no later than August 18, 2003, the Restitution Program was informed of the pendency of the Debtor's bankruptcy case. Though no additional contacts were made by the Restitution Program prior to the entry of the discharge, the record amply establishes the Program sent four letters to Debtor through her attorney's office entitled "Official Notice", "Warning Notice", "Final Notice", and "Importance Notice". The Court will not go into great detail about these letters at this juncture, however, as it is sufficient to state that they are strongly worded and promise the imposition of substantial sanctions including criminal charges unless certain conduct occurs. The last contact was made as recently as January 8, 2004, only two weeks prior to hearing in this matter and long after the filing of the Motion for Sanctions under § 362.

Debtor filed the pending Motion for Sanctions under § 362 while the automatic stay was still in effect. Debtor did not amend or allege a violation of § 524(a) during these proceedings. While there is certain appeal to the Court addressing the impact of these facts under § 524, the Court concludes that it is inappropriate to address their application without an appropriate motion by Debtor.

Therefore, the Court concludes that no relief is warranted under the original motion (§ 362). However, relief may exist under the unpled § 524(a). The Court determines that it should allow counsel for Debtor a reasonable period of time to evaluate the circumstances to determine whether to elect to amend the motion for sanctions to a request for relief under § 524(a).

WHEREFORE, for all the reasons set forth herein, the Court concludes that any violation of the automatic stay by Wal-Mart was technical in nature and inadvertent. No relief should be granted in favor of Debtor against Wal-Mart for any conduct occurring during the imposition of the automatic stay.

FURTHER, the Court concludes, for all the reasons set forth in this opinion, that American Corrective Counseling Services made contact with Debtor during the automatic stay under § 362. However, any contacts made during the time of the imposition of the automatic stay were inadvertent and were done without any notice of the pendency of Debtor's bankruptcy case. As such, the imposition of

sanctions is inappropriate against American Corrective Counseling Services under § 362.

FURTHER, the Court concludes that counsel for Debtor should be allowed until March 22, 2004 within which to amend and seek relief against American Corrective Counseling Services asserting a violation of the post-discharge injunction under § 524.

FURTHER, if Debtor elects to make such an amendment, the Court will schedule additional hearings as necessary to address these allegations.

FURTHER, if Debtor does not elect to file such an amendment, the Court will thereafter enter a final judgment consistent with this opinion.

SO ORDERED this 4th day of March, 2004.

Paul J. Kilburg
Chief Bankruptcy Judge