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# Issues Regarding the Most Effective Tool of U.S. Bankruptcy Law

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ISSUES REGARDING THE MOST EFFECTIVE TOOL OF U.S. BANKRUPTCY LAW:

‘THE AUTOMATIC STAY’

by

ZEENAT KERA

(Under the Direction of Professor Lorie Johnson)

ABSTRACT

This thesis addresses three areas in which there have been important developments concerning the automatic stay of the U.S. Bankruptcy law, provided by 11 U.S.C. § 362. The first part of the thesis addresses and analyses the question whether state courts have jurisdiction to determine their own jurisdiction when the automatic stay is at issue. The consensus, however, now seems to favor the traditional and correct view, that while bankruptcy courts alone have jurisdiction to lift or modify the stay, state courts, have jurisdiction to determine whether the stay does or does not cut off its jurisdiction to reach the merits of a case. The second topic is whether a state court has jurisdiction to impose sanctions for an alleged violation of the stay. The analysis, with the help of case laws will show that even if a state court or another federal court has jurisdiction to determine whether the stay applies, only the bankruptcy court where the case is pending has jurisdiction to impose sanctions for violating the stay. The third part of the thesis explains and analyses issues concerning repossession of property by a creditor before the filing of a bankruptcy petition.

INDEX WORDS: Automatic Stay, Issues, Jurisdiction, State Court, Bankruptcy Court, Stay Violation, Creditor, Repossession, Bankruptcy Petition

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## DEDICATION

With all my love, to Dhruv.

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## **I. INTRODUCTION TO BANKRUPTCY LAW:**

The term *bankruptcy law* is generally used to refer to federal law- title 11 of the United States Code, commonly referred to as the Bankruptcy Code.<sup>1</sup> The current law became effective October 1, 1979, after President Carter signed the Bankruptcy Reform Act of 1978 on November 1978.<sup>2</sup> This Act has been amended on many occasions, the three major amendments being the *Bankruptcy Amendments and Federal Judgeship Act of 1984; Bankruptcy Judges, United States Trustees, and Family Farmer Bankruptcy Act of 1986; and the Bankruptcy Reform Act of 1994.*<sup>3</sup>

### **Bankruptcy Code-**

The Bankruptcy Code is comprised of eight chapters that follow odd numbers- 1, 3, 5, 7, 11, and 13 with the addition of Chapter 12 for family farmers in the year 1986.<sup>4</sup> Chapters 1, 3, 5, contain provisions of general applicability in all types of bankruptcy cases.<sup>5</sup> The Chapters 7, 9, 11, 12 and 13 specify a particular type of bankruptcy case, provisions of which apply exclusively to those cases under it.<sup>6</sup> The most common type of bankruptcy case is one under Chapter 7, providing for a liquidation or sale of the debtor's assets and distribution of the net proceeds to creditors, as opposed to some form of rehabilitation of the debtor, as provided for by the remaining Chapters, i.e. Chapters 9, 11, 12, and 13.<sup>7</sup>

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<sup>1</sup> See 11 U.S.C. § 101 et. seq.

<sup>2</sup> Association of Insolvency and Restructuring Advisors, CERTIFIED INSOLVENCY AND RESTRUCTURING ADVISOR (CIRA) Study Course, 2 (Revised 2003) (unpublished CIRA study course).

<sup>3</sup> *Id.*

<sup>4</sup> Charles Jordan Tabb, THE LAW OF BANKRUPTCY, 14 (Foundation Press 1997).

<sup>5</sup> *Id.* at 14-15

<sup>6</sup> *Id.* at 15

<sup>7</sup> *Id.*

Chapter 13 is usually perceived to be the alternative to Chapter 7 for consumer debtors.<sup>8</sup>

Chapter 12 is a Chapter 13 clone, which is available to family farmers.<sup>9</sup> Chapter 11 is the basic reorganization Chapter.<sup>10</sup> Chapter 9, seldom invoked, permits the adjustments of the debts of a municipality.<sup>11</sup>

## **Bankruptcy Courts-**

### Structure:

Bankruptcy courts are federal courts with jurisdiction over cases arising under the Bankruptcy Code (Title 11 of the United States Code).<sup>12</sup> Technically, bankruptcy courts receive cases that are referred to them by the Federal District Court; thus, Federal District Courts have power to retain jurisdiction over cases arising under Title 11.<sup>13</sup>

Appeals of a bankruptcy court decision go through the trial district court first, and are then appealable through the Federal Circuit Court of Appeals and the United States Supreme Court.<sup>14</sup>

With the consent of all interested parties, appeals may also be brought to the Bankruptcy Appeals Panel, if a panel exists in the Circuit in which the appeal is made, which is generally composed of three sitting bankruptcy judges.<sup>15</sup>

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<sup>8</sup> *Id.*

<sup>9</sup> *Id.*

<sup>10</sup> *Id.*

<sup>11</sup> *Id.*

<sup>12</sup> *See* 11 U.S.C. (1994).

<sup>13</sup> 28 U.S.C. § 157 (1994).

<sup>14</sup> 28 U.S.C. § 158(b) (1994).

<sup>15</sup> *Id.*

## II. CORE PROCEEDINGS:

For a bankruptcy judge to exercise its jurisdiction over a matter, the bankruptcy judge must determine that the issues to be resolved are core proceedings.<sup>16</sup> Once an issue is determined to be a core proceeding, a bankruptcy court may issue decisions and apply non-bankruptcy law in the same manner as any other federal court.<sup>17</sup> For example, if one of the claims in a Chapter 11 case is for patent infringement, the bankruptcy court could effectively hold a trial on the issue of patent infringement within the ambit of a hearing to objections on claims.<sup>18</sup> This allows the bankruptcy court to settle most matters related to the bankruptcy estate in one courtroom. The following is a list of some of the matters considered core proceedings:

1. [M]atters concerning the administration of the estate.<sup>19</sup>
2. Allowance or disallowance of claims against the estate or exemption from the property of the estate, and estimation of claims or interests for the purpose of confirming a plan under Chapter 11, 12, or 13 of Title 11, but not the liquidation or estimation of contingent or unliquidated personal injury tort or wrongful death claims against the estate for the purposes of distribution in a case under Title 11.<sup>20</sup>
3. Counterclaims by the estate against persons filing claims against the estate.<sup>21</sup>
4. Orders to turn over property of the estate.<sup>22</sup>
5. Proceedings to determine, avoid, or recover preferences.<sup>23</sup>
6. Motions to terminate, annul, or modify the automatic stay.<sup>24</sup>
7. Proceedings to determine, avoid, or recover fraudulent conveyances.<sup>25</sup>
8. Determinations as to dischargeability of particular debts.<sup>26</sup>
9. Objections to discharges.<sup>27</sup>

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<sup>16</sup> See 28 U.S.C. § 157(b) (1994).

<sup>17</sup> See, Association of Insolvency Restructuring Advisors, *supra* note 2, at 4.

<sup>18</sup> *Id.*

<sup>19</sup> See 28 U.S.C. § 157(b)(2)(1994).

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

<sup>21</sup> *Id.*

<sup>22</sup> *Id.*

<sup>23</sup> *Id.*

<sup>24</sup> See 28 U.S.C. § 157(b)(2) (1994).

<sup>25</sup> *Id.*

<sup>26</sup> *Id.*

<sup>27</sup> *Id.*

10. Confirmations of plans.<sup>28</sup>

11. Orders approving the use or lease of property, including the use of cash collateral.<sup>29</sup>

12. Orders approving the sale of property other than property resulting from claims brought by the estate against persons who have not filed claims against the estate.<sup>30</sup>

The bankruptcy judge determines whether a matter is a core proceeding.<sup>31</sup>

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<sup>28</sup> *Id.*

<sup>29</sup> *Id.*

<sup>30</sup> *Id.*

<sup>31</sup> *See*, Association of Insolvency and Restructuring Advisors, *supra* note 2, at 5.

### **III. PROPERTY OF THE ESTATE: (11 U.S.C §§ 541, 542)**

When a voluntary petition is filed or when an order for relief is entered in an involuntary proceeding, all property of the debtor vests in a bankruptcy estate.<sup>32</sup> This includes all legal and equitable interests in property and in causes of action as well as any property recovered by the debtor-in-possession during the course of bankruptcy.<sup>33</sup> The interests of the debtor and the debtor's spouse in community property is also included in the estate if the debtor exercises any control over the property or the property was used to secure the debt that has matured into a claim against the debtor.<sup>34</sup>

The Bankruptcy Code has a very comprehensive definition of property of the estate of a debtor. Section 541(a) of the Bankruptcy Code includes in the estate all legal and equitable interests of the debtor, wherever located and by whomever held.<sup>35</sup>

Section 541(c)(1) states that property of the debtor will be included in the estate, notwithstanding any provision in an agreement or applicable non bankruptcy law that restricts or conditions such a transfer, including those that provide that property reverts to a creditor conditioned on the bankruptcy, financial condition or insolvency of the debtor.<sup>36</sup>

There is one exception to this treatment in section 541(c)(2), which states that, “a restriction on the transfer of a beneficial interest of the debtor in a trust that is enforceable under applicable

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<sup>32</sup> Questions of whether or not an item is included in the estate are almost always resolved in favor of inclusion: *See In re Richard L. Kochell*, 732 F.2d 564 (7<sup>th</sup> Cir. 1984) (IRA assets are property of the estate and can be used to satisfy debts of the estate); Under 11 U.S.C. § 542(a)(5) any property received by the debtor within 180 days of filing as an inheritance, death benefit, or a divorce settlement becomes property of the estate.

<sup>33</sup> *See* Association of Insolvency and Restructuring Advisors, *supra* note 2, at 202.

<sup>34</sup> 11 U.S.C. § 542(a)(2) (1994).

<sup>35</sup> 11 U.S.C. § 542(a) (1994).

<sup>36</sup> 11 U.S.C. § 542(c)(1) (1994).

non bankruptcy law is enforceable in a case under this title.”<sup>37</sup> The legislative history of the Bankruptcy Code indicates that this exception was intended to keep the assets of any spendthrift trust of which the debtor was a beneficiary out of the debtor’s estate in recognition of the wishes of the settler.<sup>38</sup>

While section 522 of the Bankruptcy Code allows the debtor to retain certain exempt assets, these assets go into the estate. Under that section, a decision has to be made as to whether the property qualifies for one of the exemptions under section 522 or under the applicable state law.<sup>39</sup>

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<sup>37</sup> 11 U.S.C. § 542(c)(2) (1994).

<sup>38</sup> See Association of Insolvency and Restructuring Advisors, *supra* note 2, at 203.

<sup>39</sup> See 11 U.S.C. § 522(b) (1994).

#### **IV. ADEQUATE PROTECTION: (11 U.S.C. § 361)**

##### **General Concept-**

In instances where a creditor's security interest in an asset is endangered, depreciating, or being dissipated by the debtor's actions, the creditor may move the court for adequate protection.<sup>40</sup> When a creditor seeks adequate protection, he is asking the court to ensure that the status quo will be maintained throughout the duration of the stay.<sup>41</sup> The court has broad discretion in the method it chooses to remedy adequate protection problems.

The legislative history indicates the process that the Congress intended to resolve adequate protection problems. First, the trustee or the debtor-in-possession should propose a method for providing adequate protection.<sup>42</sup> Then the creditor can accept, object or negotiate an alternative solution.<sup>43</sup> If the parties cannot reach an agreement, the court will step in to resolve the dispute.<sup>44</sup>

Though a creditor may enter an adequate protection motion with a desire to continue a foreclosure action or stop the debtor from granting an additional lien on property in which the creditor holds a security interest, the court may order an alternative remedy.<sup>45</sup> The court may require the debtor-in-possession to make cash payments to the creditor in instances where the value of the collateral is decreasing or where the amount of any security cushion is eroding

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<sup>40</sup> A motion for adequate protection can be brought under the Bankruptcy Code § 362 (relief from automatic stay), § 363 (motion to halt the use of cash collateral), or § 364 (regarding the granting of liens on previously encumbered property).

<sup>41</sup> There are three seminal cases in the adequate protection area: *In re American Mariner Industries, Inc.*, 734 F.2d 426 (9<sup>th</sup> Cir. 1984), *In re Briggs Transportation Co.*, 780 F.2d 1339 (8<sup>th</sup> Cir. 1985) & *United Savings of America v. Timbers of Inwood Forest Association*, 484 U.S. 365(1988).

<sup>42</sup> See 11 U.S.C. § 541(b)(1994).

<sup>43</sup> *Id.*

<sup>44</sup> *Id.*

<sup>45</sup> *Id.*

where interest accrues.<sup>46</sup> The court may also choose to grant relief from the stay in order to allow the creditor to seize assets in which the creditor holds a security interest.<sup>47</sup> The court must balance the danger to the interest of the creditor against the necessity of the property to the debtor in the reorganization.<sup>48</sup>

Adequate protection may be required under three Bankruptcy Code sections:

1. “Section 362 with the automatic stay—For example, unless the security interest of the debtor is adequately protected, the court may remove the stay.”<sup>49</sup>
2. “Section 363 dealing with the use (including the use of cash collateral), sale or lease of property of the debtor—For example, the court may not approve the release of cash collateral until it has been determined that the impacted creditors are adequately protected.”<sup>50</sup>
3. “Section 364 dealing with the obtaining of credit—For example, before the court might approve the granting of a senior or equal lien under the priming of a secured creditor, the court must ascertain that the creditor is adequately protected.”<sup>51</sup>

Adequate protection, according to section 361 of the Bankruptcy Code, may be provided by:

1. “Requiring the trustee or debtor-in-possession to make cash payments to the extent that the stay under section 362, or the use, sale, lease under section 363, or the grant of a lien under section 364 results in a decrease in the value of the entity’s interest in such property.”<sup>52</sup>

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<sup>46</sup> *Id.*

<sup>47</sup> *Id.*

<sup>48</sup> *Id.*

<sup>49</sup> *See* 11 U.S.C. § 362 (1994).

<sup>50</sup> *See* 11 U.S.C. § 363 (1994).

<sup>51</sup> *See* 11 U.S.C. § 364 (1994).

<sup>52</sup> *See* 11 U.S.C. § 361 (1994).

2. “Providing an additional or replacement lien to the extent that the stay, use, sale, or lease or grant results in a decrease in value of the entity’s interest in such property.”<sup>53</sup>
3. “Granting such other relief, other than entitling such entity to an administrative expense, that will result in the realization by such entity of the indubitable equivalent of the entity’s interest in such property.”<sup>54</sup>

The meaning of “indubitable equivalent” is not defined in the Bankruptcy Code. It often involves the substitute of one asset as collateral by another asset of lesser value in the case of debtor-in-possession financing.<sup>55</sup> Note that the requirement is that the debtor must have the opportunity to realize the indubitable equivalent of the entity’s interest in the property and not the value of the property.<sup>56</sup> Actually, this language has been held to refer to cases where more than one entity has an interest in the collateral. The following analysis is still true- but it is independent of the quoted language. Thus, if the creditor is adequately protected, then the debtor may be able to substitute less favorable collateral for the existing collateral.<sup>57</sup> The bankruptcy court may look at the equity cushion or analyze special risk factors in determining if the debtor is adequately protected in these cases.<sup>58</sup>

### **Equity Cushion-**

An equity cushion is the value in the property, above the amount owed to the creditor with a secured claim that will shield that creditor or claim from loss due to any decrease in the value of the property during the time the automatic stay remains in effect.<sup>59</sup>

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<sup>53</sup> See 11 U.S.C. § 361 (1994).

<sup>54</sup> *Id.*

<sup>55</sup> See Association of Insolvency and Restructuring Advisors, *supra* note 2, at 205.

<sup>56</sup> *Id.*

<sup>57</sup> *Id.*

<sup>58</sup> *Id.*

<sup>59</sup> *Id.*

Shortly after the Bankruptcy Code was enacted, a large number of courts began to evaluate the amount of the equity cushion that exists to determine if some form of adequate protection was necessary to prevent the relief from the automatic stay.<sup>60</sup> The bankruptcy court in *In re McKilips*,<sup>61</sup> analyzed prior cases and concluded that an equity cushion of less than 11 percent is sufficient and a range between 12 and 20 percent has divided the courts.<sup>62</sup>

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<sup>60</sup> See Association of Insolvency and Restructuring Advisors, *supra* note 2, at 205.

<sup>61</sup> *In re McKilips*, 81 B.R. 545 (Bankr. N.D. Ill. 1987).

<sup>62</sup> See, Association of Insolvency and Restructuring Advisors, *supra* note 2, at 205.

## V. THE AUTOMATIC STAY: (11 U.S.C. § 362)

### General Concept-

The automatic stay is an integral structural component of a U.S. bankruptcy case and is akin to a statutory injunction.<sup>63</sup> It is self-executing, effective upon the filing of a bankruptcy petition.<sup>64</sup> It is essential to the realization of two core functions of a bankruptcy case: (i) the equitable treatment of multiple creditor claims and (ii) a financial fresh start for honest debtors.<sup>65</sup> Upon the filing of a bankruptcy petition, whether voluntary or involuntary, the automatic stay of section 362 of the U.S. Bankruptcy Code comes into effect. The stay applies to all entities and essentially provides for an injunction against litigation, lien enforcement or other actions taken against a debtor or the estate to either enforce or collect pre-petition claims.<sup>66</sup> Creditors are precluded from getting a jump on their fellow creditors and the debtor is given a ‘breathing spell’ in order to enable him to reorganize.<sup>67</sup> The stay, thus seeks to preserve the status quo as of the date the bankruptcy case is commenced until such time as the bankruptcy court can act.<sup>68</sup> In addition, the stay prevents many other actions, formal or informal, which might affect property of the debtor or the estate.

The broad scope of the automatic stay is illustrated in *In re Sportfame of Ohio, Inc.*,<sup>69</sup> Defendant Wilson Sporting group refused to ship its products to debtor, Sportfame, unless

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<sup>63</sup> See Tabb, *supra* note 2, at 36.

<sup>64</sup> *Id.*

<sup>65</sup> *Id.*

<sup>66</sup> *Id.*

<sup>67</sup> *Id.* at 39-40.

<sup>68</sup> *Id.*

<sup>69</sup> *In re Sportfame of Ohio, Inc.*, 40 Bankr. 47 (N.D. Ohio 1984).

Sportfame paid off pre-petition arrearages.<sup>70</sup> While Wilson did not file any formal action against Sportfame, the conditioning of future shipments' wages upon payment of arrearages was a violation of the automatic stay.<sup>71</sup> Under the language of this case, any coercive action on the part of a creditor designed to pay a pre-petition debt can be a violation of the automatic stay.<sup>72</sup> The remedy imposed by the court was to issue a mandatory injunction requiring Wilson to ship goods to Sportfame on a normal basis.<sup>73</sup>

The following acts are expressly subject to the automatic stay under 11 U.S.C. § 362(a):

1. [T]he commencement, continuation of any judicial, administrative or other proceeding against the debtor which was or could have been commenced pre-petition, or any other proceeding to recover a claim against the debtor arising pre-petition.<sup>74</sup>
2. The enforcement of a judgment against either the debtor or the property of the estate.<sup>75</sup>
3. Any act to obtain property of the estate, and any act to exercise control over the estate.<sup>76</sup>
4. Any act to create, perfect or enforce any lien against property of the estate.<sup>77</sup>
5. Any act to create, perfect or enforce any lien against the property of the estate to the extent that the lien secures a pre-petition claim.<sup>78</sup>
6. Any act to collect, assess, or recover a claim against the debtor that arose pre-petition.<sup>79</sup>
7. The setoff of any debt owing to the debtor arising pre-petition against any claim against the debtor.<sup>80</sup>
8. The commencement or continuation of a proceeding before the United States Tax Court concerning the debtor.<sup>81</sup>

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<sup>70</sup> *Id.*

<sup>71</sup> *Id.*

<sup>72</sup> *Id.* at 56-57.

<sup>73</sup> *Id.*

<sup>74</sup> Jonathan L. Flaxer, *How to Handle Consumer Bankruptcy Cases: A Practical Step-by-Step Guide*, 52 PLI/NY, 283 (1999); see *In re Gucci*, 126 F. 3d 380 (2d Cir. 1997); *Koolik v. Markowitz*, 40 F.3d 567 (2d Cir.1994)

<sup>75</sup> See Flaxer, *supra* note 74, at 286; see *Cloughton v. Mixson*, 33 f.3d 4,5 (4<sup>th</sup> superth Cir. 1994); *In re Siskin*, 231 B.R. 514, 519 (Bankr. E.D.N.Y. 1999).

<sup>76</sup> See Flaxer, *supra* note 74, at 286; see *In re Wicks*, 176 B.R. 695 (Bankr. E.D.N.Y. 1995), *aff'd* 215 B.R. 316 (E.D.N.Y. 1997).

<sup>77</sup> See Flaxer, *supra* note 74, at 286; see *In re Layton*, 220 B.R. 508, 514 (Bankr. N.D.N.Y. 1998); *In re Ferrante*, 195 B.R. 990 (Bankr. N.D.N.Y. 1996).

<sup>78</sup> See Flaxer, *supra* note 74, at 286; see *James v. Washington Mut. Sav. Bank (In re Brooks)*, 871 F.2d 89, 90 (9<sup>th</sup> superth Cir.1989).

<sup>79</sup> See Flaxer, *supra* note 74, at 287; see *Sosne v. Reinert & Dureg, P.C. (In re Just Brakes System Inc.)*, 108 F.3d 881, 884 (8<sup>th</sup> superth Cir.1997), cert. denied, 118 S.Ct. 364, 139 L.Ed.2d 283 (1997).

<sup>80</sup> See Flaxer, *supra* note 75, at 287; see *AETNA Casualty & Surety Co. v. LTV Steel Co., Inc., (In re Chateaugay Corp.)* 94 F 3d 772, 781 (2d Cir. 1996); *Town of Hempstead Employees Fed. Credit Unoin v. Wicks*, 215 B.R. 316 (E.D.N.Y. 1997); *In re Inosphere Clubs, Inc.*, 177 B.R. 198, 207 (Bankr. S.D.N.Y. 1995).

<sup>81</sup> See Flaxer, *supra* note 74, at 287; see *In re CF & I Fabricators, Inc.*, 148 B.R. 332, 341 (Bankr. D. Utah 1992).

While the automatic stay of section 362(a) precludes many acts against the debtor or property of the estate, the following acts are excepted from the stay pursuant to section 362(b):

1. [T]he commencement or continuation of a criminal action against the debtor.<sup>82</sup>
2. The commencement or continuation of an action or proceeding to determine paternity or for the establishment or modification of an order for alimony, maintenance or support, and attempts to collect alimony, maintenance or support from property that is not property of the estate.<sup>83</sup>
3. Any act to perfect or to maintain or continue the perfection of an interest of an interest in property to the extent that the trustee's rights and powers are subject to such perfection pursuant section 546(b), or to the extent that such perfection is accomplished within the statutory period provided in section 547(e)(2)(A) of the Bankruptcy Code.<sup>84</sup>
4. The commencement or continuation of an action or proceedings by a governmental unit to enforce such governmental unit's police or regulatory power.<sup>85</sup>
5. The enforcement of a judgment, other than a money judgment, obtained by a governmental unit to enforce such governmental unit's regulatory or police power.<sup>86</sup>
6. Setoffs relating to certain securities and commodities transactions.<sup>87</sup>
7. Setoffs relating to repurchase, or "repo", agreements.<sup>88</sup>
8. The commencement of any action by the Secretary of Housing and Urban Development to foreclose a mortgage or deed of trust that is or was insured by the National Housing Act and which covers property or combinations of property consisting of five or more living units.<sup>89</sup>
9. An audit by a governmental unit to determine tax liability, the issuance of a notice of tax deficiency by a governmental unit; a demand for tax returns; or the making of an assessment for any tax and the issuance of a notice and demand for payment of such assessment.<sup>90</sup>

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<sup>82</sup> See Flaxer, *supra* note 74, at 288; see *In re Maloney*, 204 B.R. 671 (Bankr.E.D.N.Y. 1996); *In re Newman*, 196 B.R. 700, 764 (Bankr.S.D.N.Y. 1996).

<sup>83</sup> See Flaxer, *supra* note 74, at 288; see *Terio v. Terio*, 1994 W.L. 141980 (S.D.N.Y. 1994), *aff'd* 52 F. 3d 310 (2d Cir. 1995); *In re Cole*, 202 B.R. 356 (Bankr. S.D.N.Y. 1996).

<sup>84</sup> See Flaxer, *supra* note 74, at 288; see *Klien v. Civale Trovato, Inc. (In re The Lionel Corp.)*, 29 F. 3d 88 (2d Cir.1994)

<sup>85</sup> See Flaxer, *supra* note 74, at 289; See *Board of Governors of the Federal Reserve System v. MCorp Financial, Inc.*, 502 U.S. 32, 112 S.Ct. 459, 116 L.8d 2d 358 (1991).

<sup>86</sup> See Flaxer, *supra* note 74, at 289; See *State of New York v. Almy Bros., Inc.*, 1996 WL 12031 (N.D.N.Y. 1996); *In re Ngan Gung Restaurant, Inc.*, 183 B.R. 689, 691 (Bankr. S.D.N.Y. 1995).

<sup>87</sup> See Flaxer, *supra* note 74, at 289; See *Wolkowitz v. Shearson Lehman Bros., Inc. (In re Weisberg)*, 136 F.3d 655, 657 (9<sup>th</sup> superth Cir 1998).

<sup>88</sup> See Flaxer, *supra* note 74, at 290; See *Cohen v. Savings Bldg. & Loan Co. (In re Beville, Bresler, & Schulman Asset Mgt. Corp.)*, 896 F.2d 54 (3d Cir. 1990).

<sup>89</sup> 11 U.S.C. § 362(b)(8)(1994).

<sup>90</sup> See Flaxer, *supra* note 74, at 290; see *In re Carlson*, 198 B.R. 949, 953 (N.D. Ill. 1996), *aff'd*, 126 F.3d 915 (7<sup>th</sup> superth Cir. 1997), *cert. denied*. *Carlson v. United States*, 523 U.S. 1060, 118 S.Ct. 1388 (1998); *In re Neary*, 220 B.R. 864 (Bankr. E.D. Pa. 1998).

10. Any act by a lessor to the debtor under a lease of on residential real property which has expired by its terms either pre-petition or during the bankruptcy case to obtain possession of such property.<sup>91</sup>
11. The presentment of a negotiable instrument and the giving of notice of and protesting dishonor of such an instrument.<sup>92</sup>
12. &13. In a case involving a debtor subject to reorganization under Chapter 11 of the Bankruptcy Code, after ninety days after the petition date, the commencement or continuation, and conclusion to the final judgment, of an action to foreclose a ship or fleet mortgage or a mortgage or other interest in a fishing facility held by the Secretary of Transportation or Secretary of Commerce.<sup>93</sup>
14. Any action by an accrediting agency regarding the accreditation status of the debtor as an educational facility.<sup>94</sup>
15. Any action by a State licensing body regarding the licensure of the debtor as an educational institution.<sup>95</sup>
16. Any action by a guaranty agency regarding the eligibility of the debtor to participate in programs under the Higher Education Act of 1965.<sup>96</sup>
17. The setoff by a swap participant of any mutual debt and claim in connection with certain swap agreements.<sup>97</sup>
18. The creation or perfection of a statutory lien for an ad valorem property tax.<sup>98</sup>

The automatic stay of any act against property generally remains in effect unless such property is no longer property of the estate.<sup>99</sup> The stay of any other act listed in the Bankruptcy Code § 362(a) remains in effect until the earlier of the time the case is closed, the time the case is dismissed or, the time the debtor receives a discharge.<sup>100</sup>

The court may terminate, annul, modify or condition the automatic stay upon the request of a party in interest if there is a cause, such as a lack of adequate protection of that party's interest in property, or, with respect to stay of an act against property under the Bankruptcy Code § 362(a), if the debtor has no equity in the property and the property is not necessary to an effective

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<sup>91</sup> See Flaxer, *supra* note 74, at 291; see *In re Salzer*, 52 F.3d 708 (7<sup>th</sup> Cir. 1995), cert. denied, *Salzer v. Stinson*, 516 U.S. 1177, 116 S.Ct. 1273 (1996).

<sup>92</sup> See Flaxer, *supra* note 74, at 291; see *In re Mills*, 176 B.R. 924, 928 (D. Kan. 1994); *In re Jastrem*, 224 B.R. 125 (Bankr. E.D. Ca. 1998).

<sup>93</sup> See Flaxer, *supra* note 74, at 291; see *Adams v. S/V "Tenacious"*, 203 B.R. 297 (D. Alaska 1996).

<sup>94</sup> See Flaxer, *supra* note 74, at 292; See *In re Statewide Oilfield Construction Co., Inc.*, 134 B.R. 399 (Bankr. E.D. Cal. 1991).

<sup>95</sup> See 11 U.S.C. § 362(b)(15) (1994).

<sup>96</sup> See Flaxer, *supra* note 75, at 292; see *In re Betty Owen Schools, Inc.*, 195 B.R. 23, 31 (Bankr. S.D.N.Y. 1996).

<sup>97</sup> See 11 U.S.C. § 362(b)(17)(1994).

<sup>98</sup> See Flaxer, *supra* note 74, at 292; *In re Merry-Go-Round Enters., Inc.*, 227 B.R. 775 (Bankr. D. Md. 1998).

<sup>99</sup> See Flaxer, *supra* note 74, at 293.

<sup>100</sup> *Id.*

reorganization.<sup>101</sup> If the court should rule upon a party's request for relief from an automatic stay of an act against property of the estate within thirty days after the request, the stay is automatically terminated as to the party making the request, unless the court, after notice and a hearing, orders otherwise.<sup>102</sup>

The party requesting relief from the stay bears the burden of proof on the issue of the debtor's equity in the property.<sup>103</sup> The debtor bears the burden of proof on all other issues.<sup>104</sup> If any individual is injured by any willful violation of the automatic stay, that individual may recover actual damages including costs, attorneys' fees, and in some cases, punitive damages as well.<sup>105</sup>

Section 362(h) of the Bankruptcy Code provides for relief from the stay. Section 362(h) states: "Any individual injured by the 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."<sup>106</sup>

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<sup>101</sup> 11 U.S.C. § 362(d) (1994).

<sup>102</sup> 11 U.S.C. § 362(e)(1994).

<sup>103</sup> 11 U.S.C. § 362(g)(1994).

<sup>104</sup> *Id.*

<sup>105</sup> 11 U.S.C. § 362(h)(1994).

<sup>106</sup> *Id.*

## **VI. AUTOMATIC STAY ISSUES:**

### **Introduction-**

The automatic stay is fundamental to the bankruptcy process, and only the bankruptcy court in which the case is pending has jurisdiction to grant or deny relief from the stay.<sup>107</sup> The point of contention is whether a state court or more generally, a non bankruptcy tribunal has jurisdiction to determine whether the stay applies in the first instance, and what effect should be given to a judgment rendered when the non bankruptcy forum decides, perhaps erroneously, that the stay does not apply.<sup>108</sup> The question comes down to whether state courts have jurisdiction to determine their own jurisdiction when the stay is at issue. Federal courts have been divided on this question.<sup>109</sup> The consensus, however, now seems to favor the traditional view that, while bankruptcy courts alone have jurisdiction to lift or modify the stay, state courts like non bankruptcy federal courts, have jurisdiction to determine whether the stay does or does not cut off the tribunal's jurisdiction to reach the merits of the case.<sup>110</sup> Federal courts should be bound by a state court ruling in this respect.<sup>111</sup>

A second and related topic is whether a state court, or more generally, any forum, other than the bankruptcy court where a case is pending, has jurisdiction to impose sanctions for an alleged violation of the stay. Although this question has not arisen frequently, the weight of

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<sup>107</sup> See *Farley v. Henson*, 2 F. 3d 273 (8<sup>th</sup> Cir 1993); *In re Gullett*, 230 B.R. 231 (Bankr. S.D. Tex. 1999).

<sup>108</sup> David B. Young, *Automatic Stay Issues: Selected Developments*, 838 PLI/Comm9, 17 (2002) .

<sup>109</sup> See *Raymark Indus., Inc., v. Lai*, 973 F.2d 1125 (3d Cir. 1992); *Kalb v. Fuerstein*, 308 U.S. 433 (1940); *In re Rainwater*, 233 B.R. 126 (Bankr. N.D. Ala. 1999), vacated, 254 B.R. 273 (N.D. Ala. 2000) (each case holding that state courts do not have jurisdiction to determine whether the stay applies); See *In re Singleton*, 230 B.R. 533 (6<sup>th</sup> Cir. B.A.P. 1999); *In re Glass*, 240 B.R. 782 (Bankr. M.D. Fla. 1999); *In re Siskin*, 258 B.R. 554 (Bankr. E.D.N.Y. 2001) (each of the cases holding that state courts do have jurisdiction to determine whether the automatic stay applies in proceedings before them).

<sup>110</sup> See Young, *supra* note 108, at 17.

<sup>111</sup> *Id.*

authority now holds that, even if a state court or another federal court has jurisdiction to determine whether the stay applies, only the bankruptcy court where the case is pending has jurisdiction to call a party to task for violating the stay.<sup>112</sup> This follows from the more general principle that only a court seized of a case may impose sanctions for interference with that court's orders or process.<sup>113</sup>

A third type of stay dispute has arisen particularly in the context of consumer bankruptcies.<sup>114</sup> If a creditor has lawfully repossessed a debtor's property before filing of the bankruptcy petition (pre-petition), but if the property has not been sold or title has not been passed, so that the debtor still retains rights in the property, courts have disagreed strongly as to whether the creditor violates the stay, by simply retaining the property until adequate protection is provided.<sup>115</sup> Some courts have held that the creditor has an absolute duty to turn over the property regardless of adequate protection, and hence that the creditor violates the stay if this is not done.<sup>116</sup> Others have held that merely retaining the property does not violate the stay and that the creditor has no duty to surrender the property until adequate protection is given.<sup>117</sup>

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<sup>112</sup> See, e.g., *Halas v. Platek*, 239 B.R. 784 (N.D. Ill. 1999); *Hawthorne v. Hameed*, 836 P.2d 683 (Okla. Ct. App. 1989); *Gonzales v. Parks*, 830 F.2d 1033 (9<sup>th</sup> Cir. 1987), *In re Harrison*, 185 B.R. 607 (Bankr. D. Kan. 1995) (These cases held that federal courts must have exclusive jurisdiction over stay violations).

<sup>113</sup> See *Young*, *supra* note 108, at 18.

<sup>114</sup> *Id.*

<sup>115</sup> See *In re Bunton*, 246 B.R. 851 (Bankr. N.D. Ohio 2000); *In re Berscheidt*, 223 B.R. 579 (Bankr. D. Wyo. 1998); *In re Brooks*, 207 B.R. 738 (Bankr. N.D. Fla. 1997); *In re Sharon*, 200 B.R. 181 (Bankr. S.D. Ohio 1996) (holding that creditor violates the automatic stay by retaining possession of the (debtor's) property); See, e.g., *In re Spears*, 223 B.R. 159 (Bankr. N.D. Ill. 1998); *In re Fitch*, 217 B.R. 286 (Bankr. S.D. Cal. 1998); *In re Young*, 193 B.R. 620 (Bankr. D.D.C. 1996); *In re Deiss*, 166 B.R. 92 (Bankr. S.D. Tex. 1994) (holding that the creditor does not violate the automatic stay merely by retaining possession of the vehicle or other property, and that the creditor is under no obligation to turn over the property unless and until the court so orders and adequate protection is provided).

<sup>116</sup> See *Brooks*, 207 B.R. 783; *Sharon*, 200 B.R. 18; *In re Del mission, Ltd.*, 98 F.3d 1147 (9<sup>th</sup> Cir. 1996)

<sup>117</sup> See *Spears*, 223 B.R. 159; *Fitch*, 217 B.R. 286; *Deiss*, 166 B.R. 92.

## **(a) Do State Courts Have Jurisdiction To Determine Their Own Jurisdiction When The Automatic Stay Is At Issue?**

### Overview of the problem:

A bankruptcy court where a case is pending has exclusive original jurisdiction to grant or deny relief from the stay.<sup>118</sup> No other court may do so as an original matter.<sup>119</sup> Although bankruptcy courts have exclusive original jurisdiction to grant relief from the stay, it is universally conceded that other federal courts may decide whether the stay applies to them in a case before them.<sup>120</sup> If a lower federal court erroneously decides that the stay does not apply and proceeds to render a judgment that judgment is not subject to collateral attack.<sup>121</sup> The only remedy is by way of direct appeal.<sup>122</sup> If the reviewing federal court decides that the stay did apply, the proper step for the higher court to take is not to reverse the judgment, or even to reach to the merits of the case.<sup>123</sup> The reviewing court, should, rather vacate the judgment on the ground that the stay deprived the lower court of jurisdiction to render any judgment at all.<sup>124</sup>

The area of dispute has been whether the same principles apply to state courts. The majority rule has been that state courts like non bankruptcy federal courts, have jurisdiction to decide whether a stay applies in a pending action.<sup>125</sup> If a lower state court erroneously holds that the stay does not apply and proceeds to render a judgment, the proper course is not to attack the

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<sup>118</sup> See, e.g., *Henson*, 2 F.3d 273; *Gullett*, 230 B.R. 231.

<sup>119</sup> *Id.*

<sup>120</sup> See Young, *supra* note 108, at 20; See, also, *N.L.R.B. v. Edward Cooper painting, Inc.*, 804 F.2d 934 (6<sup>th</sup> Cir. 1985); *S.E.C. v. Bilzerian*, 131 F. Supp. 2d 10 (D.D.C. 2001).

<sup>121</sup> See Young, *supra* note 108, at 20.

<sup>122</sup> *Id.*

<sup>123</sup> See Young, *supra* note 108, at 20.

<sup>124</sup> *Chao v. Hospital Staffing Servs., Inc.*, 270 F.3d 374 (6<sup>th</sup> Cir. 2001) (vacating judgment of the United States District Court for the Western District of Tennessee because action was subject to the stay of a bankruptcy case pending in Florida; cause remanded with instructions to dismiss for want of subject matter jurisdiction).

<sup>125</sup> See Jeffery H. Gallet & Robert Z. Dobrish, *The Bankruptcy Automatic Stay: It's Not the End of the World—or of the Case*, 16 J.Am. ACAD. MATRIM.LAW. 149 (1999); See, e.g., *In re Martinez*, 227 B.R. 442 (Bankr. D.N.H. 1998).

judgment collaterally.<sup>126</sup> Rather, relief should be sought in a higher state court, and ultimately, if necessary, in the United States Supreme Court.<sup>127</sup>

A few cases have, however, held that the state courts do not even have jurisdiction to determine whether the stay applies.<sup>128</sup> Thus, a state appellate court would lack jurisdiction to correct the errors of a lower court in this respect because state reviewing courts, like state trial courts, lack jurisdiction to decide the applicability of the stay.<sup>129</sup> Therefore, state court judgments allegedly rendered in violation of the stay are subject to collateral review in the bankruptcy court.<sup>130</sup> If the bankruptcy court decides that the stay was violated, it may disregard, or even vacate, the state court's judgment.<sup>131</sup> The bankruptcy court's decision that the stay did or did not apply to the state court action would then be subject to direct review in the federal judicial system.<sup>132</sup>

Cases holding that the state courts lack jurisdiction to determine whether the stay applies:

1. **Raymark Indus., Inc. v Lai**<sup>133</sup>

*Raymark Indus., Inc. v Lai*<sup>134</sup> was one of the early cases to imply that state courts do not have jurisdiction to decide whether the stay applies.<sup>135</sup> There, a products liability plaintiff had obtained a judgment against Raymark Industries in a California court.<sup>136</sup> Raymark had paid a

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<sup>126</sup> *Id.*

<sup>127</sup> *Id.*

<sup>128</sup> See *Raymark Indus.*, 973 F.2d 1125; *Fuerstein*, 308 U.S. 433 (1940); *Rainwater*, 233 B.R. 126 (each case holding that state courts do not have jurisdiction to determine whether the stay applies)

<sup>129</sup> See Young, *supra* note 108, at 21.

<sup>130</sup> *Id.*

<sup>131</sup> *Id.*

<sup>132</sup> *Id.*

<sup>133</sup> *Raymark Indus.*, 973 F.2d 1125.

<sup>134</sup> *Id.*

<sup>135</sup> *Id.*

<sup>136</sup> *Id.*

deposit into court to stay the execution of the judgment.<sup>137</sup> Subsequently, an involuntary bankruptcy petition was filed against Raymark in the Eastern district of Pennsylvania.<sup>138</sup> Although Raymark had been preparing an appeal in the tort case, Raymark contended that the entire proceeding was subject to the automatic stay.<sup>139</sup> Relying on bankruptcy precedents to the effect that an action against a pre-petition deposit into court did not violate the stay, the bankruptcy court held that the stay did not apply, and the district court affirmed.<sup>140</sup>

Furthermore, Raymark had not transmitted the complete record to the California Court of Appeals, maintaining that the stay barred any further action in the lawsuit.<sup>141</sup> The state appellate court dismissed Raymark's appeal for want of diligent prosecution.<sup>142</sup> In the appeal from the decision of the lower federal courts, the Third Circuit reversed the district court and the bankruptcy court and held that the state court proceeding was stayed by virtue of 11 U.S.C. § 362(a).<sup>143</sup> The Third Circuit held that reliance on bankruptcy precedents was misplaced.<sup>144</sup> This reversal of the lower federal court's decision presented no remarkable jurisdictional issues.

In the present case, the Third Circuit Court chose to address the decision of the California Court of Appeals dismissing Raymark's appeal.<sup>145</sup> The Third Circuit conceded that with exceptions not relevant to the case at bar, lower federal courts have no jurisdiction to collaterally review the merits of a state court decision.<sup>146</sup> The Third Circuit, however, maintained that a federal court may collaterally review a state court's express or implied determination of its own

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<sup>137</sup> *Id.*

<sup>138</sup> *Id.* at 1128.

<sup>139</sup> *Id.* at 1129-1130.

<sup>140</sup> *Id.*

<sup>141</sup> *Id.* at 1127.

<sup>142</sup> *Id.*

<sup>143</sup> *Id.* at 1127.

<sup>144</sup> *Id.*

<sup>145</sup> *Id.*

<sup>146</sup> *Id.*

jurisdiction.<sup>147</sup> The Third Circuit held that state actions taken in violation of the stay are void ab initio.<sup>148</sup> The state appellate court's decision to dismiss the debtor's appeal was based on a mistaken conclusion that the stay did not apply.<sup>149</sup> The Third Circuit, thus concluded that the decision of the California Court of Appeals was void.<sup>150</sup> The federal court remanded the case with directions to the bankruptcy court to vacate the judgment of the state appellate court and thus to reinstate the state court appeal.<sup>151</sup>

The *Raymark Indus.*<sup>152</sup> decision was noteworthy in its holding that a federal bankruptcy court had the authority to render an order vacating the decision of a state court of appeals.<sup>153</sup> The decision, however, offered no real explanation as to why a federal court may not collaterally review the merits of a state court decision but why nonetheless it may review a state court's decision as to its own jurisdiction.<sup>154</sup> The only explanation that would make the *Raymark Indus.*<sup>155</sup> holding coherent is that the state court has no jurisdiction to determine whether the stay applies.<sup>156</sup> Thus, when a state court's judgment allegedly violates the stay, a bankruptcy court should conduct a de novo review of that question.<sup>157</sup> If the bankruptcy court determines independently that the stay does not apply, then it must give full faith and credit to the state court judgment on the merits.<sup>158</sup> If, however the stay did apply, then the bankruptcy court should vacate the judgment without reference to the merits.<sup>159</sup>

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<sup>147</sup> *Id.* at 1131.

<sup>148</sup> *Id.*

<sup>149</sup> *Id.*

<sup>150</sup> *Id.*

<sup>151</sup> *Id.* at 1131-32

<sup>152</sup> *Raymark Indus. Inc.*, 973 F.2d 1125.

<sup>153</sup> *Id.* at 1132.

<sup>154</sup> *See Young, supra* note 108, at 23.

<sup>155</sup> *Raymark Indus.Inc.*,, 973 F.2d 1125.

<sup>156</sup> *See Young, supra* note 108, at 24.

<sup>157</sup> *Id.*

<sup>158</sup> *Id.*

<sup>159</sup> *Id.*

For several years *Raymark Indus.*<sup>160</sup> was something of an anomaly, and it aroused relatively little attention.<sup>161</sup> It was a series of decisions from the Ninth Circuit that thrust to the fore the question of state court jurisdiction to determine the applicability of the stay.<sup>162</sup>

## 2. *The Ninth Circuit's Decision in In re Gruntz*<sup>163</sup>

*In re Gruntz*<sup>164</sup> involved the criminal prosecution and conviction of the debtor, Robert Gruntz for failure to pay child support.<sup>165</sup> The District Attorney of the Los Angeles County had sought and obtained a conviction under section 270 of the California Penal Code.<sup>166</sup> Both in the state trial court and on appeal, Gruntz had argued that the courts of California had no jurisdiction because the action violated the automatic stay 11 U.S.C. § 362(a)(1) (prohibiting the commencement or continued prosecution of any action against the debtor that was begun or could have begun before the commencement of the case).<sup>167</sup> The state court of appeals held that the case fell squarely within the scope of 11 U.S.C. § 362(b)(1), which exempts from the stay the commencement or continuation of any criminal action or proceeding against the debtor.<sup>168</sup> After his state court convictions were final, Gruntz filed an adversary proceeding in the bankruptcy court seeking to nullify the criminal convictions on the ground that the state court courts lacked jurisdiction to decide that 11 U.S.C. § 362(b)(1) applied, particularly in light of *Hucke v. State of Oregon*.<sup>169</sup> The bankruptcy court dismissed Gruntz's complaint on res judicata grounds, noting

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<sup>160</sup> *Raymark Indus. Inc.*, 973 F.2d 1125.

<sup>161</sup> *See Young, supra* note 108, at 25.

<sup>162</sup> *See Young, supra* note 108, at 25.

<sup>163</sup> *In re Gruntz*, 166 F.3d 1020 (9<sup>th</sup> Cir.) (“Gruntz I”), opinion amended and superseded on reh’g, 177 F.3d 728 (9<sup>th</sup> Cir. ) (“Gruntz II”), reh’g en banc granted, opinion withdrawn, 177 F.3d 729 (9<sup>th</sup> Cir. 1999), opinion on reh’g, 202 F.3d 1074 (9<sup>th</sup> Cir. 2000) (“Gruntz III”).

<sup>164</sup> *Id.*

<sup>165</sup> *Gruntz I*, 166 F.3d 1020.

<sup>166</sup> *Id.*

<sup>167</sup> *Id.*

<sup>168</sup> *Id.* at 1023.

<sup>169</sup> *Hucke v. State of Oregon*, 992 F.2d 950 (9<sup>th</sup> Cir.), cert. denied, 510 U.S. 862 (1993) (In this case, the debtor had been convicted of a felony and placed on probation. After the debtor had filed for a chapter 13 petition, his probation had been revoked, allegedly because, among other reasons, he had failed to make restitutionary payments.

that the applicability of the stay had been presented to and been rejected by the California court and was the same affirmed by the district court.<sup>170</sup>

In two sharply divided panel opinions, the Ninth Circuit reversed and held that the bankruptcy court had jurisdiction to decide whether the stay applied and to collaterally review the state court convictions.<sup>171</sup> The majority in both panel opinions held that the state court determination that the stay applied was in no way binding on federal courts, and that the bankruptcy court could disregard the fact that the state court had erred and the stay did not apply.<sup>172</sup> The majority held that neither the Rooker-Feldman doctrine<sup>173</sup> nor preclusion applies when rendering forum has acted in the absence of all jurisdiction; and, according to panel majorities, only the bankruptcy court has initial jurisdiction to determine whether the stay applies at all.<sup>174</sup>

In sharp dissents in both panels, Judge Fletcher maintained that the California courts had already decided that the stay did not apply and hence that they had jurisdiction over the criminal prosecution.<sup>175</sup>

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The debtor then turned to the bankruptcy court to seek release. The debtor maintained that the revocation of his probation was an attempt to collect or recover a pre-petition claim in violation of 11 U.S.C. § 362(a)(6). The bankruptcy court ruled in the debtor's favor and the district court affirmed. In the Ninth Circuit, the State of Oregon argued that the revocation of the debtor's probation was exempted from the stay by 11 U.S.C. § 362(b)(1). The Ninth Circuit agreed in part with both sides. Normally, the revocation proceeding would be shielded by 11 U.S.C. § 362(b)(1), which exempts the commencement or continuation of a criminal action from the automatic stay. The Ninth Circuit, held, however, that this exception does not apply when the object of the criminal proceeding is to compel the debtor to pay a pre-petition debt. Examining the record, the panel then concluded that the revocation of the debtor's probation in the case before them was not in fact designed to force the debtor to pay the pre-petition restitution obligation).

<sup>170</sup> *Gruntz I*, 166 F.3d 1020.

<sup>171</sup> *Gruntz II*, 177 F.3d at 8-9.

<sup>172</sup> *Gruntz II*, 177 F.3d at 9.

<sup>173</sup> See *District of Columbia Court of Appeals v. Feldman*, 460 U.S. 462 (1983); *Rooker v. Fidelity Trust Co.*, 263 U.S. 413 (1923) (under the Rooker- Feldman doctrine, the general rule is that no federal court except the Supreme Court has jurisdiction to review a state court decision. While there are exceptions to the Rooker –Feldman doctrine the district court determined that none of them applied).

<sup>174</sup> *Id.*

<sup>175</sup> 177 F.3d at 15-16.

On February 3, 2000, the Ninth Circuit handed down its final decision in *Gruntz* in a unanimous ruling.<sup>176</sup> The Ninth Circuit reiterated the earlier holdings of the panel majorities that federal courts are not bound in any fashion by a state court ruling when the state court has acted in absence of all jurisdiction.<sup>177</sup> In such a case, the state court judgment is a nullity and the Rooker-Feldman doctrine does not apply.<sup>178</sup> The *Gruntz*<sup>179</sup> court, however, framed the issue not as to whether a state court has jurisdiction to determine whether the stay applies, but rather as whether a state court has jurisdiction to grant relief from the stay.<sup>180</sup> The court pointed out that granting relief from the stay is a core matter and the court then came to the unremarkable conclusion that only the bankruptcy court in which the bankruptcy case is pending has jurisdiction as an initial matter to vacate, annul, modify or lift the stay.<sup>181</sup> The court went on to state that a federal court should examine the motives for a state court prosecution only in the rarest and most egregious circumstances.<sup>182</sup>

The Ninth Circuit in *In re Durbar*,<sup>183</sup> held squarely that no state tribunal, whether judicial or administrative, has jurisdiction to decide whether the stay applies.<sup>184</sup> Original jurisdiction over that question is vested exclusively in the non-bankruptcy court where the case is pending.<sup>185</sup> According to *Dunbar*,<sup>186</sup> then if a state forum takes some action that allegedly violates the stay, that decision is always open to collateral review in the bankruptcy court, even if the state court

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<sup>176</sup> See *Gruntz III*, 202 F.3d 1074.

<sup>177</sup> *Id.*

<sup>178</sup> *Id.* at 1075.

<sup>179</sup> *Gruntz*, 166 F.3d 1020 (9<sup>th</sup> Cir.) (“*Gruntz I*”), opinion amended and superseded on reh’g, 177 F.3d 728 (9<sup>th</sup> Cir.) (“*Gruntz II*”), reh’g en banc granted, opinion withdrawn, 177 F.3d 729 (9<sup>th</sup> Cir. 1999), opinion on reh’g, 202 F.3d 1074 (9<sup>th</sup> Cir. 2000) (en banc) (“*Gruntz III*”).

<sup>180</sup> *Gruntz III*, 202 F.3d at 1077.

<sup>181</sup> *Id.*

<sup>182</sup> *Id.*

<sup>183</sup> *In re Durbar*, 245 F.3d 1058 (9<sup>th</sup> Cir. 2001).

<sup>184</sup> See *id.* at 1061-62.

<sup>185</sup> *Id.*

<sup>186</sup> *Dunbar*, 245 F.3d 1058.

has declared that the stay does not apply.<sup>187</sup> The bankruptcy court's examination must be de novo.<sup>188</sup> If the bankruptcy court determines independently that the stay does not apply, then it must give full faith and credit to the state tribunal's decision on the merits.<sup>189</sup> If however, the bankruptcy court determines independently that the stay did apply, then the bankruptcy court should enjoin the enforcement of the state forum's orders, vacate the state decision, or otherwise refuse to extend full faith and credit.<sup>190</sup>

### 3. *In re Rainwater*<sup>191</sup>

In *Rainwater*, an Alabama state court had revoked the debtor wife's probation post-petition, following her pre-petition conviction for theft.<sup>192</sup> The bankruptcy court issued a writ of habeas corpus, awarded declaratory and injunctive relief, and refused to award damages.<sup>193</sup> The most important aspect of the *Rainwater*<sup>194</sup> decision was that the court held that the stay barred the revocation proceeding and that a federal court could collaterally review the state court's decision.<sup>195</sup> The bankruptcy court held that a criminal prosecution or a probation proceeding is not exempted from the stay if the purpose of the action is to enforce or collect a claim or a debt, and that restitution falls into that category.<sup>196</sup> The court held that the state court lacked subject matter jurisdiction over the underlying action because of the stay; that a state court judgment rendered under such circumstances was not entitled to full faith and credit; and that the Rooker-Feldman doctrine did not apply because of the lack of jurisdiction.<sup>197</sup>

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<sup>187</sup> See Young, *supra* note 108, at 33.

<sup>188</sup> *Id.* at 34.

<sup>189</sup> See *In re Motley*, 268 B.R. 237 (Bankr. C.D. Cal 2001) (discussing *Dunbar* and *Gruntz*)

<sup>190</sup> *Id.*

<sup>191</sup> *In re Rainwater*, 233 B.R. 126 (Bankr. N.D. Ala. 1999).

<sup>192</sup> *Id.*

<sup>193</sup> *Id.* at 127.

<sup>194</sup> *Rainwater*, 233 B.R. 126.

<sup>195</sup> See Young, *supra* note 108, at 35.

<sup>196</sup> See *Rainwater*, 233 B.R. 129.

<sup>197</sup> *Id.* at 130.

The district court vacated the bankruptcy court's judgment on appeal.<sup>198</sup> The court did not reach the question of full faith and credit, or, of the applicability of the Rooker Feldman doctrine.<sup>199</sup> Rather, the district court emphasized the strong policy against federal interference with state court criminal proceedings and rejected the idea that there is a debt collection exception to 11 U.S.C. § 362 (b)(1).<sup>200</sup>

Cases holding that state courts have jurisdiction to determine whether the stay applies and that federal courts are barred from collateral review of such jurisdictional decisions:

1. *In re Singleton*<sup>201</sup>

In *In re Singleton*<sup>202</sup>, the Ohio state court had decided that neither 11 U.S.C. § 362 nor the co-debtor stay, (11 U.S.C. §1301), protected the property of a corporation owned by the Chapter 13 debtor, and the state court had ordered the sale of the debtor's property.<sup>203</sup> The debtor did not seek review before an Ohio state Appellate court, but rather commenced an adversary proceeding in a bankruptcy court in an effort to nullify the state court judgment and the sale.<sup>204</sup> The bankruptcy court dismissed the complaint for failure to state a claim, and the bankruptcy appellate panel affirmed.<sup>205</sup>

The *Singleton*<sup>206</sup> court never discussed whether the state court had correctly interpreted the Bankruptcy Code; rather the panel held that a lower federal tribunal lacked subject matter

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<sup>198</sup> Bryan v. Rainwater, 254 B.R. 273 (N.D. Ala. 2000).

<sup>199</sup> See Young, *supra* note 108, 36.

<sup>200</sup> *Id.*

<sup>201</sup> *In re Singleton*, 230 B.R. 533 (6<sup>th</sup> Cir. B.A.P. 1999).

<sup>202</sup> *Id.*

<sup>203</sup> See Young, *supra* note 108, at 37.

<sup>204</sup> See *Singleton*, 230 B.R. at 535.

<sup>205</sup> *Id.*

<sup>206</sup> *Id.* at 533.

jurisdiction to address that question at all.<sup>207</sup> The state court had jurisdiction to decide whether the stay applied, even though the state court lacked jurisdiction to lift or modify the stay.<sup>208</sup> For a federal court to revisit the question whether the stay applied would amount to usurping the functions of a state appellate court.<sup>209</sup> The debtor's proper remedy would have been to appeal to a higher court in Ohio, and ultimately to seek review before the United States Supreme Court, if necessary.<sup>210</sup> The debtor had failed to follow that course, and a lower federal court could only dismiss the action.<sup>211</sup>

## 2. *In re Siskin*<sup>212</sup>

In *In re Siskin*,<sup>213</sup> creditors had obtained pre-petition judgments against the debtor in the courts of New York.<sup>214</sup> The debtor had refused to cooperate with examinations in aid of execution, or otherwise, obey court orders.<sup>215</sup> After the bankruptcy petition was filed, the judgment creditors sought and obtained a contempt order and an order of commitment from a state court.<sup>216</sup> The debtor contended that the proceedings violated the stay, 11 U.S.C. §§ 362(a)(1), (2), (6), but the state court rejected the argument.<sup>217</sup> The debtor was incarcerated briefly and sought a writ of habeas corpus from the United States district court for the Eastern District of New York.<sup>218</sup> The habeas corpus action was rendered moot when the debtor was released from confinement.<sup>219</sup>

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<sup>207</sup> *Id.* at 536.

<sup>208</sup> *Id.*

<sup>209</sup> *Id.*

<sup>210</sup> *Id.* at 537

<sup>211</sup> *Id.*

<sup>212</sup> *In re Siskin*, 258 B.R. 554 (Bankr. E.D.N.Y. 2001).

<sup>213</sup> *Id.*

<sup>214</sup> *Id.*

<sup>215</sup> *Id.* at 555.

<sup>216</sup> *Id.* at 557.

<sup>217</sup> *Id.*

<sup>218</sup> *See id.*

<sup>219</sup> *See id.* at 557-558.

The debtor then commenced adversary proceeding in the bankruptcy court seeking sanctions against the creditors and their attorneys for a willful violation of the stay.<sup>220</sup> Initially, the bankruptcy court had agreed that the stay had been violated.<sup>221</sup> The defendants, however, maintained that the state court had already made a decision that the stay did not apply to the contempt proceeding, and that the bankruptcy court was precluded from revisiting that question.<sup>222</sup> The bankruptcy court agreed and dismissed the adversary proceeding.<sup>223</sup> The debtor moved for reconsideration, asking the court to adopt the Ninth Circuit’s reasoning in *Gruntz*.<sup>224</sup>

In the opinion on reconsideration, the bankruptcy court rejected *Gruntz*,<sup>225</sup> and adhered to its earlier decision to dismiss the action seeking sanctions.<sup>226</sup> The *Siskin*<sup>227</sup> court reasoned that 28 U.S.C. § 1334(a), does not give bankruptcy courts the authority to determine whether the stay applies, and there is no principled reason to say that state courts do not have the same authority.<sup>228</sup> If the state court makes an erroneous decision as to the applicability of the stay- i.e., as to its own jurisdiction, the proper remedy is to seek relief in a higher state tribunal, not to ask a federal bankruptcy court to slip into the robes of a state appellate court.<sup>229</sup> The state court had made an explicit or implicit decision that the stay did not apply.<sup>230</sup> The *Siskin*<sup>231</sup> court held that

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<sup>220</sup> *Id.*

<sup>221</sup> *Id.*

<sup>222</sup> *Id.*

<sup>223</sup> *Id.*

<sup>224</sup> *Gruntz*, 166 F.3d 1020 (9<sup>th</sup> Cir.) (“*Gruntz I*”), opinion amended and superseded on reh’g, 177 F.3d 728 (9<sup>th</sup> Cir. ) (“*Gruntz II*”), reh’g en banc granted, opinion withdrawn, 177 F.3d 729 (9<sup>th</sup> Cir. 1999), opinion on reh’g, 202 F.3d 1074 (9<sup>th</sup> Cir. 2000) (en banc) (“*Gruntz III*”).

<sup>225</sup> *Id.*

<sup>226</sup> *See Siskin*, 258 B.R. at 559.

<sup>227</sup> *Id.*

<sup>228</sup> *See Siskin*, 258 B.R. 554.

<sup>229</sup> *Id.*

<sup>230</sup> *Id.*

<sup>231</sup> *See Siskin*, 258 B.R. 554.

under the Rooker-Feldman doctrine, a federal court lacked jurisdiction to collaterally review that determination.<sup>232</sup>

The *Siskin*<sup>233</sup> court noted that the contempt power lies at the very heart of the authority of a state judicial system to vindicate the dignity and integrity of its own courts.<sup>234</sup> If any tribunal should interfere with or overturn a contempt order, it should be a higher court with the same judicial system, not a federal bankruptcy court.<sup>235</sup>

### 3. *In re Glass*<sup>236</sup>

In *In re Glass*<sup>237</sup> the court gave an analysis very much like the bankruptcy appellate panel's analysis in *Singleton*<sup>238</sup> and rejected the reasoning of both, the majority in *Gruntz I*<sup>239</sup> and the *Rainwater*.<sup>240</sup> In this case, the debtor brought an adversary proceeding seeking damages from his former wife and her attorneys for an alleged stay violation.<sup>241</sup> The former wife had pursued a post-petition action in a Georgia court to hold the debtor in contempt for failure to pay support pursuant to a divorce decree.<sup>242</sup> The debtor had raised the stay issue, but the state court had held that the action fell within the scope of 11 U.S.C. § 362(b)(2)(A)(ii), which exempts from the stay, the commencement or continuation of any action for the establishment or modification of an order for alimony, maintenance, or support.<sup>243</sup> The *Glass*<sup>244</sup> court refused to revisit the Georgia court's decision concerning the stay.<sup>245</sup> Instead, like the *Singleton*<sup>246</sup> panel,

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<sup>232</sup> *Id.*

<sup>233</sup> *Id.*

<sup>234</sup> *Id.*

<sup>235</sup> *Id.*

<sup>236</sup> *In re Glass*, 240 B.R. 782 (Bankr. M.D. Fla. 1999).

<sup>237</sup> *Id.*

<sup>238</sup> *Singleton*, 230 B.R. 533

<sup>239</sup> *Gruntz*, 166 F.3d at 1020.

<sup>240</sup> *Rainwater*, 233 B.R. 126.

<sup>241</sup> *Young*, *supra* note 108, at 37-38.

<sup>242</sup> *Id.*

<sup>243</sup> *Id.*

<sup>244</sup> *Id.*

<sup>245</sup> *Id.*

the *Glass*<sup>247</sup> court held that it lacked subject matter jurisdiction to decide whether the court had adjudicated the issue correctly.<sup>248</sup> The debtor was asking the bankruptcy court to sit as a state appellate court, and this was impermissible.<sup>249</sup> Alternatively, the debtor was attempting to attack the state court decision collaterally, which was likewise impermissible.<sup>250</sup>

Analysis supporting the view that state courts have jurisdiction to determine whether the stay applies:

The analysis as to why state courts should have jurisdiction to determine whether the stay applies to matters brought before it should begin by understanding the jurisdictional statute- 28 U.S.C. § 1334, and its effects.

1. 28 U.S.C. § 1334 and its effects

Title 28 U.S.C. § 1334, states:

(a) [E]xcept as provided in sub-section (b) of this section, the district courts shall have original and exclusive jurisdiction of all cases under Title 11.

(b) “ Notwithstanding any act of Congress that confers exclusive jurisdiction on a court or courts other than the district courts, the district courts shall have original but not exclusive jurisdiction of all civil proceedings arising under Title 11, or arising in or related to cases under Title 11.”<sup>251</sup>

The Ninth Circuit in *Gruntz*<sup>252</sup> and in *Dunbar*<sup>253</sup> interpreted 28 U.S.C. § 1334, by stating that the same was a jurisdiction- divesting statute.<sup>254</sup> The *Rainwater*<sup>255</sup> court had reached the

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<sup>246</sup> *Singleton*, 230 B.R. 533.

<sup>247</sup> *Glass*, 240 B.R. 782.

<sup>248</sup> *Young*, *supra* note 108, at 38.

<sup>249</sup> *Id.*

<sup>250</sup> *Id.*

<sup>251</sup> 28 U.S.C. § 1334 (1994).

<sup>252</sup> *Gruntz*, 166 F.3d 1020 (9<sup>th</sup> Cir.) (“Gruntz I”), opinion amended and superseded on reh’g, 177 F.3d 728 (9<sup>th</sup> Cir. ) (“Gruntz II”), reh’g en banc granted, opinion withdrawn, 177 F.3d 729 (9<sup>th</sup> Cir. 1999), opinion on reh’g, 202 F.3d 1074 (9<sup>th</sup> Cir. 2000) (en banc) (“Gruntz III”).

<sup>253</sup> *Dunbar*, 245 F.3d 1058.

<sup>254</sup> *See Young*, *supra* note 108, at 43.

<sup>255</sup> *Rainwater*, 233 B.R. 126.

same conclusion as well.<sup>256</sup> However, this statutory interpretation is mistaken.<sup>257</sup> 28 U.S.C. § 1334(a) vests district courts- and, by referral under 28 U.S.C. § 157(a),<sup>258</sup> bankruptcy courts, with original and exclusive jurisdiction over bankruptcy cases.<sup>259</sup> It is undoubted that this statute deprives state courts of jurisdiction over bankruptcy cases, but that is beside the point.<sup>260</sup>

The courts in *Siskin*<sup>261</sup> and *Glass*,<sup>262</sup> pointed out that 28 U.S.C. § 1334(a) is not relevant in determining whether state courts have jurisdiction to decide whether the automatic stay applies.<sup>263</sup> A proceeding to determine whether the stay applies to a given action is not “a case under Title 11”, over which bankruptcy courts have ‘original and exclusive’ jurisdiction under 28 U.S.C. § 1334(a).<sup>264</sup> Moreover, the underlying state courts actions in all the cases discussed above were not “cases under Title 11.”<sup>265</sup> Both, the *Siskin*<sup>266</sup> and the *Glass*<sup>267</sup> court noted that the pertinent jurisdictional statute is 28 U.S.C. § 1334(b), which vests bankruptcy courts with original, but not exclusive jurisdiction over “all civil proceedings arising under Title 11 or arising in, or related to cases under Title 11.”<sup>268</sup> The *Siskin*<sup>269</sup> and the *Glass*<sup>270</sup> courts, therefore, properly held that a proceeding to determine whether the stay applies at all is a proceeding arising in or under the Bankruptcy Code or that is related to a bankruptcy case.<sup>271</sup>

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<sup>256</sup> See *id.* at 131-32.

<sup>257</sup> See Young, *supra* note 108, at 43.

<sup>258</sup> 28 U.S.C. § 157(a) provides: “Each district court may provide that any or all cases under title 11 and any or all proceedings arising under title 11 or arising in or related to a case under title 11 shall be referred to the bankruptcy judges for the district.”

<sup>259</sup> 28 U.S.C. § 1334(a)(1994).

<sup>260</sup> See Young, *supra* note 108, 43.

<sup>261</sup> *Siskin*, 258 B.R. 554.

<sup>262</sup> *Glass*, 240 B.R. 782.

<sup>263</sup> See *Siskin*, 258 B.R. at 559; See *Glass*, 240 B.R. at 793-94.

<sup>264</sup> See *id.*

<sup>265</sup> *Id.*

<sup>266</sup> *Siskin*, 258 B.R. 554 .

<sup>267</sup> *Glass*, 240 B.R. 782 .

<sup>268</sup> See 28 U.S.C. § 1334(b) (1994).

<sup>269</sup> *Siskin*, 258 B.R. 554.

<sup>270</sup> *Glass*, 240 B.R. 782.

<sup>271</sup> See Young, *supra* note 108, at 44.

Another case which deserves mention and discussion here, is *Andria D. Powell v. Washington Land Co., INC.*<sup>272</sup> In this case, an appeal was brought to the District of Columbia Court of Appeals from the decision of the Superior Court of Washington.<sup>273</sup> Here, the Appellant was a tenant under a lease managed by the landlord, the Washington land company.<sup>274</sup> The Landlord and Tenant Branch of the Superior Court of the District of Columbia had entered a default judgment against the Appellant and her husband, granting the landlord possession of the property and the landlord then filed a writ of execution on the judgment against the Appellant.<sup>275</sup> Eight days later, the appellant filed for bankruptcy under Chapter 13 of the U.S. Bankruptcy Code in the U.S. bankruptcy Court of the District of Columbia.<sup>276</sup> Three days later, the agents of the landlord attempted to evict the Appellant, pursuant to the Writ of Execution.<sup>277</sup> The Appellant then filed a complaint in the D.C. Superior Court alleging wrongful eviction, violation of automatic stay resulting from the bankruptcy filing, and conversion.<sup>278</sup> The trial court dismissed the complaint for lack of subject-matter jurisdiction and the appellant/debtor appealed.<sup>279</sup>

The bankruptcy jurisdiction granted to the district courts by 28 U.S.C. § 1334(a) and (b) may be transferred to the bankruptcy court under 28 U.S.C. § 157.<sup>280</sup> Section 157(b) allows the bankruptcy court to hear and decide cases as to which the district court has exclusive jurisdiction under § 1334(a) (cases under “Title 11”) as well as “core proceedings” as to which the district

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<sup>272</sup> *Andria D. Powell v. Washington Land Co., Inc.*, 684 A.2d 769 (D.C.1995).

<sup>273</sup> *See id.*

<sup>274</sup> *Id.*

<sup>275</sup> *Id.*

<sup>276</sup> *Powell.*, 684 A.2d at 770.

<sup>277</sup> *Id.*

<sup>278</sup> *Id.*

<sup>279</sup> *Id.*

<sup>280</sup> 28 U.S.C. § 157(a) provides: “Each district court may provide that any or all cases under title 11 and any or all proceedings arising under title 11, or arising in or related to a case under title 11 shall be referred to the bankruptcy judges for the district.”

court has original, but not exclusive jurisdiction under § 1334(b) (proceedings “arising under Title 11” or arising in a case under Title 11.”)<sup>281</sup> The District of Columbia Court of Appeals determined that in the context of the Bankruptcy Code’s jurisdictional statutory scheme, the narrow issue was whether the complaint filed by the Appellant in the Superior Court was a “case under Title 11” over which the U.S. District Court (or bankruptcy court) had exclusive jurisdiction.<sup>282</sup> If it was so, the Superior court would have no jurisdiction to hear the claim and the court would have properly dismissed the Appellant’s complaint.<sup>283</sup> If not, the Superior Court would have jurisdiction because even if the claim could have been brought in U.S. District Court, as a proceeding “arising under Title 11” over which the U.S. District Court (or bankruptcy court) had original but not exclusive jurisdiction, the statute did not require that the claim be brought in a federal court.<sup>284</sup>

The court, in holding that that the appellant’s claim for wrongful eviction, for violation of the stay, and for conversion were within the Superior Court’s jurisdiction<sup>285</sup>, partly relied on the explanation of the jurisdictional provisions, provided by the court in *In re Brady, Texas, Mun. Gas Corp.*<sup>286</sup> which stated : “Although the district courts ‘have original and exclusive jurisdiction of all cases under Title 11,’ the district courts do not have ‘exclusive jurisdiction of all civil proceedings arising under Title 11 or arising in or related to cases under Title 11.’ Thus, under § 1334, the only aspect of the bankruptcy proceeding over which the district courts and their bankruptcy units have exclusive jurisdiction is the bankruptcy petition itself.”<sup>287</sup>

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<sup>281</sup> 28 U.S.C. § 157(b)(1) provides: “Bankruptcy judges may hear and determine all cases under title 11 and core proceedings arising under title 11, or arising in a case under title 11, referred under subsection (a) of this section, and may enter appropriate orders and judgments, subject to review under section 158 of this title.”

<sup>282</sup> See *Powell*, 684 A.2d at 772; See 28 U.S.C. § 1334(a) (West Supp. 1991).

<sup>283</sup> *Powell*, 684 A.2d at 770.

<sup>284</sup> *Id.* at 772; See 28 U.S.C. § 1334(b) (West Supp.1991).

<sup>285</sup> *Powell*, 684 A. 2d at 773.

<sup>286</sup> *In re Brady , Texas, Mun. Gas Corp.*, 936 F.2d 212, 218 (5<sup>th</sup> Cir. 1991).

<sup>287</sup> *Id*; See, e.g. *In re Wood*, 825 F.2d 90, 92 (5<sup>th</sup> Cir. 1987).

“In other matters arising in or relating to Title 11 cases, unless the Code provides otherwise, state courts have concurrent jurisdiction. . . .”<sup>288</sup>

The *Dunbar*<sup>289</sup> decision and all the three *Gruntz*<sup>290</sup> opinions reasoned that the stay is fundamental to a bankruptcy court’s exclusive jurisdiction over a bankruptcy case, and hence that, by extension, bankruptcy jurisdiction over all stay issues should be exclusive.<sup>291</sup> As Judge Fletcher pointed out in his dissents in *Gruntz I*<sup>292</sup> and *Gruntz II*<sup>293</sup>, however, courts may not use policy considerations to rewrite statutes, and as a general rule, policy concerns alone cannot cut off state court jurisdiction unless Congress has chosen to enact that policy.<sup>294</sup>

Nothing in 28 U.S.C. § 1334, and certainly nothing in 11 U.S.C. § 362, purports to deprive a state court of jurisdiction to determine whether the automatic stay applies.<sup>295</sup> A judgment rendered in violation of the stay might be a nullity if a state court simply ignored the stay or was not aware of it, but that does not mean that a determination by a non- bankruptcy tribunal that the stay does not apply in the first instance would be a nullity.<sup>296</sup>

## 2. Rooker- Feldman Doctrine

The Rooker- Feldman doctrine is based on two Supreme Court rulings separated by 60 years, *District of Columbia Court of Appeals v. Feldman*<sup>297</sup> and *Rooker v. Fidelity Trust Co.*<sup>298</sup> The gist of the doctrine is that lower federal courts lack jurisdiction to review a state court

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<sup>288</sup> *Powell*, 684 A.2d at 774.

<sup>289</sup> *See Dunbar*, 245 F.3d 1058.

<sup>290</sup> *See Gruntz*, 166 F.3d 1020 (9<sup>th</sup> Cir.) (“Gruntz I”), opinion amended and superseded on reh’g, 177 F.3d 728 (9<sup>th</sup> Cir. ) (“Gruntz II”), reh’g en banc granted, opinion withdrawn, 177 F.3d 729 (9<sup>th</sup> Cir. 1999), opinion on reh’g, 202 F.3d 1074 (9<sup>th</sup> Cir. 2000) (en banc) (“Gruntz III”).

<sup>291</sup> *See Id.*; *See Dunbar*, 245 F.3d 1058 .

<sup>292</sup> *See Gruntz I*, 166 F.3d 1020.

<sup>293</sup> *See Gruntz II*, 177 F.3d 729.

<sup>294</sup> *See Young*, *supra* note 108, at 45

<sup>295</sup> *See Haines*, *Ninth Circuit Divests State Court of Jurisdiction*, WEST’S BANKR. NEWSLTR., May 5, 1999.

<sup>296</sup> *Id.*

<sup>297</sup> *See Feldman*, 460 U.S. 462 (1983); *See Fidelity Trust Co.*, 263 U.S. 413 (1923).

<sup>298</sup> *See Id.*

judgment; such jurisdiction belongs only to the Supreme Court.<sup>299</sup> In particular, lower federal courts may not review a state court decision for errors in construing or applying federal law if the state court actually decided the federal issue or if the alleged errors are “inextricably intertwined” with the state court judgment.<sup>300</sup> A claim in the federal court is inextricably intertwined with a state court judgment if the relief requested in the federal forum would effectively nullify the state court ruling, or if the claim in the federal court could succeed only to the extent that the federal tribunal determined that the state court had erroneously decided the issues before it.<sup>301</sup>

The Rooker-Feldman doctrine is related to principles of full faith and credit, 28 U.S.C. § 1738, and to res judicata (claim preclusion) and collateral estoppel (issue preclusion).<sup>302</sup> Whereas the claim and issue preclusive effects of state court judgments are affirmative defenses that may be waived and that have nothing to do with a federal court’s jurisdiction, Rooker-Feldman is a jurisdictional doctrine that declares that a lower federal court may not usurp the functions of a state appellate court or of the Supreme Court.<sup>303</sup> Even if the federal court would otherwise have jurisdiction to consider the issue as an original matter, the federal court is divested of jurisdiction if a state court has already decided.<sup>304</sup> Thus, as it is jurisdictional, the Rooker-Feldman doctrine should be applied even before reaching the question of res judicata or collateral estoppel.<sup>305</sup>

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<sup>299</sup> See *Atlantic Coast Line R.R. Co. v. Brotherhood of Locomotive Eng’rs*, 398 U.S. 281 (1970); *In re Kelley*, 262 B.R. 307 (Bankr. E.D. Pa. 2001); See also 28 U.S.C.A. §§ 1257, 1331, 1334 (West Supp. 1991).

<sup>300</sup> See *In re Popkin & Stern*, 259 B.R. 701 (8<sup>th</sup> Cir. B.A.P. 2001).

<sup>301</sup> See *Safety Kleen, Inc. (Pinewood) v. Wyche*, 274 F.3d 806 (4<sup>th</sup> Cir. 2001).

<sup>302</sup> See *Stern*, 259 B.R. 701.

<sup>303</sup> See Adam McLain, *Comment, The Rooker- Feldman Doctrine: Toward A Workable Role*, 149 U. PA. L. REV. 1555 (2001); See also *Hachamovitch v. DeBuono*, 159 F.3d 687 (2<sup>nd</sup> Cir. 1998).

<sup>304</sup> *In re Mendez*, 246 B.R. 14 (Bankr. D.P.R. 2000); see *In re Roussos*, 251 B.R. 86 (9<sup>th</sup> Cir. B.A.P. 2000).

<sup>305</sup> See *Singleton*, 230 B.R. at 533.

The *Siskin*,<sup>306</sup> *Singleton*,<sup>307</sup> as well as the dissent in two panel decisions in *Gruntz*<sup>308</sup> relied primarily on the Rooker- Feldman doctrine to conclude that a federal court may not disturb a state court determination that the automatic stay does not apply.<sup>309</sup> The *Rainwater*<sup>310</sup> court, however, denied that the Rooker- Feldman doctrine could shield a state court decision concerning the stay from nullification.<sup>311</sup>

The question raised in *Dunbar*,<sup>312</sup> *Gruntz*,<sup>313</sup> *Singleton*,<sup>314</sup> *Siskin*,<sup>315</sup> *Glass*,<sup>316</sup> and *Rainwater*<sup>317</sup> was precisely whether a state court determination that the stay did not apply cut off a lower federal court's authority to revisit that question, or to sit, in essence, as a reviewing court.<sup>318</sup> The *Singleton*,<sup>319</sup> *Siskin*,<sup>320</sup> and *Glass*<sup>321</sup> courts gave thorough discussions of exceptions to the Rooker-Feldman doctrine and properly concluded that none of those exceptions applied.<sup>322</sup> First, the Rooker-Feldman doctrine does not apply when the statute vests exclusive jurisdiction in federal courts or a particular class of federal courts and when a state court simply ignores or defies the statute.<sup>323</sup> For example, a state court judgment purporting to lift, modify, or annul

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<sup>306</sup> *Siskin*, 258 B.R. 554 .

<sup>307</sup> *Singleton*, 230 B.R. 533.

<sup>308</sup> *Gruntz*, 166 F.3d 1020 (9<sup>th</sup> Cir.) (“Gruntz I”), opinion amended and superseded on reh’g, 177 F.3d 728 (9<sup>th</sup> Cir. ) (“Gruntz II”), reh’g en banc granted, opinion withdrawn, 177 F.3d 729 (9<sup>th</sup> Cir. 1999), opinion on reh’g, 202 F.3d 1074 (9<sup>th</sup> Cir. 2000) (“Gruntz III”).

<sup>309</sup> See Young, *supra* note 109, at 53-54.

<sup>310</sup> *Rainwater*, 233 B.R. 126.

<sup>311</sup> See *id.*

<sup>312</sup> *Dunbar*, 245 F.3d 1058.

<sup>313</sup> *Gruntz*, 166 F.3d 1020 (9<sup>th</sup> Cir.) (“Gruntz I”), opinion amended and superseded on reh’g, 177 F.3d 728 (9<sup>th</sup> Cir. ) (“Gruntz II”), reh’g en banc granted, opinion withdrawn, 177 F.3d 729 (9<sup>th</sup> Cir. 1999), opinion on reh’g, 202 F.3d 1074 (9<sup>th</sup> Cir. 2000) (“Gruntz III”).

<sup>314</sup> *Singleton*, 230 B.R. 533.

<sup>315</sup> *Siskin*, 258 B.R. 554 .

<sup>316</sup> *Glass*, 240 B.R. 782.

<sup>317</sup> *Rainwater*, 233 B.R. 126.

<sup>318</sup> See Young, *supra* note 108, at 53.

<sup>319</sup> *Singleton*, 230 B.R. 533.

<sup>320</sup> *Siskin*, 258 B.R. 554.

<sup>321</sup> *Glass*, 240 B.R. 782.

<sup>322</sup> See Young, *supra* note 108, at 54.

<sup>323</sup> *Id.*; see Fuerstein, 308 U.S. 433, 435.

the stay would be void ab initio.<sup>324</sup> The void ab initio exception to Rooker-Feldman is very narrowly construed, however.<sup>325</sup>

Second, the doctrine does not apply if a federal statute specifically grants lower federal courts the right to review state court judgments.<sup>326</sup> For example, 28 U.S.C. §§ 2241, 2254 authorize federal district courts to review state court decisions on habeas corpus proceedings.<sup>327</sup> The Rooker- Feldman would be irrelevant in such an instance.<sup>328</sup> Further, there is no comparable bankruptcy statute.<sup>329</sup>

Third, the doctrine does not prevent the review of a state court judgment that was procured by fraud, deception, accident or mistake.<sup>330</sup> For example, if the debtor or another party had actively concealed the existence of a bankruptcy case, from a state court, and if the state court had then rendered the judgment against the debtor post-petition, a bankruptcy court could disregard the judgment.<sup>331</sup> No such fraud, deception or mistake appears to have been involved in any of the cases discussed above.

Fourth, the doctrine has been held inapplicable when the party seeking relief in a federal court does not have any reasonable opportunity to present his or her federal claim or defense in state court.<sup>332</sup> In such a case, the federal issue could not be considered inextricably intertwined with the state court judgment.<sup>333</sup>

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<sup>324</sup> See Young, *supra* note 108, at 54.

<sup>325</sup> *Id.*

<sup>326</sup> *Id.*

<sup>327</sup> *Id.*; See McLain, *supra* 303, at 1555; See also Young v. Murphy, 90 F.3d 1225 (7<sup>th</sup> Cir. 1996); See U.S.C. §§ 2241, 2254.

<sup>328</sup> *Id.*

<sup>329</sup> See Young, *supra* note 108, at 54.

<sup>330</sup> *Id.*; See also *In re Sun Valley Foods Co.*, 801 F.2d 186 (6<sup>th</sup> Cir. 1986).

<sup>331</sup> See Young, *supra* note 108, at 55.

<sup>332</sup> *Id.* at 54; See also Wood v. Orange County, 715 F.2d 1543 (11<sup>th</sup> Cir. 1983).

<sup>333</sup> *Id.*

Lastly, the Rooker-Feldman doctrine will not bar a federal action by someone who was not a party to a state court action or in privity with the party, and who, thus could not have raised the federal issue or sought state court appellate review.<sup>334</sup> In the cases at issue here, these exceptions did not come into play. The debtors were parties to the state court action and were able to raise the automatic stay issue before the state tribunals.

Since no exception to the Rooker-Feldman doctrine applied, the bankruptcy appellate panel in *Singleton*,<sup>335</sup> and the bankruptcy courts in *Siskin*<sup>336</sup> and *Glass*<sup>337</sup> correctly decided that lower federal courts lacked jurisdiction to entertain the attacks of the debtors on the respective state court judgments.<sup>338</sup> Only state appellate courts, or, ultimately the Supreme Court could review whether the state trial courts had interpreted 11 U.S.C. § 362 correctly.<sup>339</sup> The bankruptcy court's opinion in *Dunbar*,<sup>340</sup> *Gruntz*,<sup>341</sup> and *Raymark*<sup>342</sup> were simply erroneous and would mistakenly allow lower federal courts to sit as appellate tribunals to review state court decisions.<sup>343</sup>

### 3. **Full Faith and Credit and Preclusion**

The Full Faith and Credit statute, 28 U.S.C. § 1738, requires a federal court to give a state court's judgment the same preclusive effects that they would be given by courts in the rendering state.<sup>344</sup> The courts have repeatedly held that when a state court has determined that the automatic stay does not apply to an action pending in that forum, then the issue of the state

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<sup>334</sup> *Young*, *supra* note 108, at 55; *See also In re Gross*, 217 F.3d 208 (4<sup>th</sup> Cir. 2000).

<sup>335</sup> *Singleton*, 230 B.R. 533.

<sup>336</sup> *Siskin*, 258 B.R. 554.

<sup>337</sup> *Glass*, 240 B.R. 782.

<sup>338</sup> *See Young*, *supra* note 108, at 55.

<sup>339</sup> *Id.*

<sup>340</sup> *Dunbar*, 245 F.3d 1058.

<sup>341</sup> *Gruntz*, 166 F.3d 1020 (9<sup>th</sup> Cir.) (“Gruntz I”), opinion amended and superseded on reh’g, 177 F.3d 728 (9<sup>th</sup> Cir. ) (“Gruntz II”), reh’g en banc granted, opinion withdrawn, 177 F.3d 729 (9<sup>th</sup> Cir. 1999), opinion on reh’g, 202 F.3d 1074 (9<sup>th</sup> Cir. 2000) (“Gruntz III”).

<sup>342</sup> *Raymark Indus. Inc.*, 973 F.2d 1125.

<sup>343</sup> *Young*, *supra* note 108, at 55.

<sup>344</sup> *See* 28 U.S.C.A. § 1738 (West Supp. 1991).

court's jurisdiction over the underlying action and the applicability of the stay may not be relitigated in a federal tribunal.<sup>345</sup> Reconsideration of the question of the applicability of the stay is barred by collateral estoppel (issue preclusion).<sup>346</sup> A state court has jurisdiction to determine its own jurisdiction, and the reconsideration of jurisdictional issues such as the stay is subject to preclusion just like other issues.<sup>347</sup> The merits of the judgment in the underlying state court case, in turn, may not be relitigated under principles of res judicata (claim preclusion).<sup>348</sup>

The panel majorities in the first two *Gruntz*<sup>349</sup> rightly acknowledged that the relitigation of jurisdictional issues may be barred, and that the jurisdiction of the first court may be shielded from collateral attack, even if the original court made an arguably erroneous determination that it had subject matter jurisdiction.<sup>350</sup> The *Gruntz*<sup>351</sup> panel majorities, however, maintained that this principle applied only when the original forum had undertaken an express examination of grounds for its jurisdiction.<sup>352</sup> Although the state courts in *Gruntz*<sup>353</sup> had decided that the automatic stay did not apply, they had apparently not made an explicit determination that they had jurisdiction to make such a decision or to construe 11 U.S.C. § 362.<sup>354</sup> Therefore, according

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<sup>345</sup> See *In re Bona*, 124 B.R. 11 (S.D.N.Y. 1991); *In re Mann*, 88 B.R. 427 (Bankr. S.D. Fla. 1998) (noting that the debtor had placed the stay question squarely before the state court and that state court had rejected the debtor's position).

<sup>346</sup> Young, *supra* note 108, at 56.

<sup>347</sup> *Id.*; See also *In re Cummings*, 201 B.R. 586 (Bankr. S.D. Fla. 1996).

<sup>348</sup> Young *supra* note 108, at 56; See also *In re Martinez*, 227 B.R. 442 (Bankr. D.N.H. 1998); *In re Weller*, 189 B.R. 467 (Bankr. E.D. Wis. 1995).

<sup>349</sup> *Gruntz*, 166 F.3d 1020 (9<sup>th</sup> Cir.) ("Gruntz I"), opinion amended and superseded on reh'g, 177 F.3d 728 (9<sup>th</sup> Cir.) ("Gruntz II"), reh'g en banc granted, opinion withdrawn, 177 F.3d 729 (9<sup>th</sup> Cir. 1999), opinion on reh'g, 202 F.3d 1074 (9<sup>th</sup> Cir. 2000) ("Gruntz III").

<sup>350</sup> Young, *supra* note 108, at 56; See also *Durfee v. Duke*, 375 U.S. 106 (1963).

<sup>351</sup> *Gruntz*, 166 F.3d 1020 (9<sup>th</sup> Cir.) ("Gruntz I"), opinion amended and superseded on reh'g, 177 F.3d 728 (9<sup>th</sup> Cir.) ("Gruntz II"), reh'g en banc granted, opinion withdrawn, 177 F.3d 729 (9<sup>th</sup> Cir. 1999), opinion on reh'g, 202 F.3d 1074 (9<sup>th</sup> Cir. 2000) ("Gruntz III").

<sup>352</sup> Young, *supra* note 108, at 56.

<sup>353</sup> *Gruntz*, 166 F.3d 1020 (9<sup>th</sup> Cir.) ("Gruntz I"), opinion amended and superseded on reh'g, 177 F.3d 728 (9<sup>th</sup> Cir.) ("Gruntz II"), reh'g en banc granted, opinion withdrawn, 177 F.3d 729 (9<sup>th</sup> Cir. 1999), opinion on reh'g, 202 F.3d 1074 (9<sup>th</sup> Cir. 2000) ("Gruntz III").

<sup>354</sup> Young, *supra* note 108, at 57.

to the panel majorities in *Gruntz I*<sup>355</sup> and *Gruntz II*<sup>356</sup>, the reconsideration of the state court's subject matter jurisdiction was not precluded.<sup>357</sup> The *Dunbar*<sup>358</sup> court had held that for relevant purposes, the distinction between the Rooker- Feldman and preclusive doctrines was immaterial.<sup>359</sup> If a state tribunal had no jurisdiction to decide whether the stay applied, its decision concerning the stay would be entitled to no deference under any theory.<sup>360</sup>

There is no general requirement that a state court must expressly examine its jurisdiction to determine its own jurisdiction.<sup>361</sup> Moreover, a party that has had a reasonable opportunity to raise the question of jurisdictional defects before the rendering forum and relied to do so may not thereafter raise subject matter jurisdiction in a collateral attack, even if the rendering forum did not explicitly address the jurisdictional issues.<sup>362</sup> Thus, a party who claims that 11 U.S.C. § 362 bars an action in a bankruptcy forum must raise all arguments connected with that contention in the rendering court or on direct appeal, not in a collateral attack.<sup>363</sup> This reasoning may not apply if a state court had rendered judgment while simply ignoring or defying a federal statute ousting it of jurisdiction.<sup>364</sup> That was not the case in *Dunbar*<sup>365</sup> or any of the other relevant cases.

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<sup>355</sup> *Gruntz I*, 166 F.3d 1020.

<sup>356</sup> *Gruntz II*, 177 F.3d 729.

<sup>357</sup> Young, *supra* note 108, at 57.

<sup>358</sup> *Dunbar*, 245 F.3d 1058.

<sup>359</sup> *See id.* at 1061.

<sup>360</sup> *Id.*

<sup>361</sup> Young, *supra* note 108, at 57.

<sup>362</sup> *Id.*; *See also* Insurance Corp. of Ireland, Ltd. v. Compagnie des Bauxities de Guinee, 456 U.S. 694 (1982).

<sup>363</sup> *Pico v. Global Marine Drilling Co.*, 900 F.2d 846 (5<sup>th</sup> Cir. 1990); *see also* *Chico County Drainage Dist.*, 308 U.S.

<sup>364</sup> *See* *Fuerstein*, 308 U.S. 433; *see also* *Rainwater*, 233 B.R. 126.

<sup>365</sup> *Dunbar*, 245 F.3d 1058.

#### 4. The weight of case-law

Before *Gruntz*<sup>366</sup> scarcely any court of appeals had held that state courts lack jurisdiction to determine whether the stay applies, or that 28. U.S.C. § 1334(a) gives bankruptcy courts exclusive jurisdiction over that question.<sup>367</sup> The only possible exception was *Raymark*,<sup>368</sup> and that court did not cite any statutory basis for its holding.<sup>369</sup> Prior to 1999, the court of appeals that had addressed the issue had held that non-bankruptcy tribunals had concurrent jurisdiction to determine whether the stay applied, and hence to decide whether they had subject matter jurisdiction to proceed with the cases pending before them.<sup>370</sup> The Third Circuit and the Second Circuit courts had also accepted this view.<sup>371</sup> The lower courts in the Ninth Circuit had agreed prior to *Gruntz*<sup>372</sup> and *Dunbar*<sup>373</sup> that non-bankruptcy courts have concurrent jurisdiction to determine the applicability of the stay.<sup>374</sup>

The overwhelming majority of lower courts that have considered the issue have held that state courts have jurisdiction to determine whether the automatic stay applies.<sup>375</sup> Lower courts in the Second Circuit, which are bound by *In re Baldwin- United Corp. Litg.*,<sup>376</sup> have taken this

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<sup>366</sup> *Gruntz*, 166 F.3d 1020 (9<sup>th</sup> Cir.) (“Gruntz I”), opinion amended and superseded on reh’g, 177 F.3d 728 (9<sup>th</sup> Cir. ) (“Gruntz II”), reh’g en banc granted, opinion withdrawn, 177 F.3d 729 (9<sup>th</sup> Cir. 1999), opinion on reh’g, 202 F.3d 1074 (9<sup>th</sup> Cir. 2000) (“Gruntz III”).

<sup>367</sup> See Young, *supra* note 108, at 46.

<sup>368</sup> *Raymark Indus. Inc.*, 973 F.2d 1125.

<sup>369</sup> Young, *supra* note 108, at 46.

<sup>370</sup> See *N.L.R.B. v. Edward Cooper Painting, Inc.*, 804 F.2d 934 (6<sup>th</sup> Cir. 1986); *In re Baldwin- United Corp. Litig.*, 765 F.2d 343 (2d Cir. 1985) (“The court in which the litigation claimed to be stayed is pending has jurisdiction to determine not only its own jurisdiction but also the more precise question whether the proceedings before it is subject to the automatic stay.”)

<sup>371</sup> See *Baldwin* 765 F.2d 343 (2d Cir. 1985); see *Brock v. Morysville body Works, Inc.*, 829 F.2d 383 (3d. Cir. 1987).

<sup>372</sup> *Gruntz*, 166 F.3d 1020 (9<sup>th</sup> Cir.) (“Gruntz I”), opinion amended and superseded on reh’g, 177 F.3d 728 (9<sup>th</sup> Cir. ) (“Gruntz II”), reh’g en banc granted, opinion withdrawn, 177 F.3d 729 (9<sup>th</sup> Cir. 1999), opinion on reh’g, 202 F.3d 1074 (9<sup>th</sup> Cir. 2000) (“Gruntz III”).

<sup>373</sup> *Dunbar*, 245 F.3d 1058.

<sup>374</sup> Young, *supra* note 108, at 47.

<sup>375</sup> *Id.*

<sup>376</sup> *Baldwin*, 765 F.2d 343.

position.<sup>377</sup> *In re Bona*,<sup>378</sup> and in *Siskin*<sup>379</sup>, the courts expressly rejected the notion that the *Baldwin*<sup>380</sup> holding was limited to federal courts.<sup>381</sup> In the Sixth Circuit, where *N.L.R.B. v. Edward Cooper Painting, Inc.*,<sup>382</sup> state courts are deemed to have concurrent jurisdiction.<sup>383</sup> In the Eleventh Circuit, the *Rainwater*<sup>384</sup> court's position that state courts may not determine the applicability of the stay is contrary to the holdings of other lower courts in that jurisdiction.<sup>385</sup> Other bankruptcy courts in the Eleventh Circuit have consistently maintained that they are bound by state court determinations as to whether the stay applied to state court proceedings.<sup>386</sup> Lower courts in other circuits have also held that state courts have concurrent jurisdiction to adjudicate the applicability of the stay, and that federal courts may not attack such determination collaterally.<sup>387</sup>

#### **(b) Do State Courts (Or Other Non-Bankruptcy Tribunals) Have Jurisdiction To Impose Sanctions For An Alleged Violation Of The Automatic Stay?**

A second and related topic is whether a state court, or, more generally, any forum other than where the bankruptcy case is pending, has jurisdiction to impose sanctions for an alleged violation of the stay.

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<sup>377</sup> Young, *supra* note 108, at 47.

<sup>378</sup> *See Bona*, 124 B.R. 11.

<sup>379</sup> *Siskin*, 258 B.R. 554.

<sup>380</sup> *Baldwin*, 765 F.2d 343.

<sup>381</sup> Young, *supra* note 108, at 49.

<sup>382</sup> *Edward Cooper Painting, Inc.*, 804 F.2d 934.

<sup>383</sup> Young, *supra* note 108, at 49.

<sup>384</sup> *Rainwater*, 233 B.R. 126.

<sup>385</sup> Young, *supra* note 108 at 49.

<sup>386</sup> *Id.*; *see also Mann*, 88 B.R. 427 (Bankr. M.D. Fla. 1999); *Cummings*, 201 B.R. 586 (Bankr. S.D. Fla. 1996).

<sup>387</sup> Young, *supra* note 108, at 49; *See Martinez*, 227 B.R. 442 (Bankr. D.N.H. 1998); *Weller*, 189 B.R. 467 (Bankr. E.D. Wis. 1995).

Following are few cases that address this issue:

1. **Daniel Hawthorne v. Akhtar Hammed**<sup>388</sup>

In this case, a collection agency, Oklahoma Collection Bureau (“OCB”), obtained a default judgment against Hawthorne in an Oklahoma state court, based on his failure to pay medical bills to Akhtar Hammed.<sup>389</sup> OCB then began garnishing the wages of Hawthorne.<sup>390</sup> Hawthorne filed for bankruptcy some six months later, triggering an automatic stay.<sup>391</sup> Nonetheless, OCB, allegedly lacking notice of Hawthorne’s bankruptcy, began garnishing its wages, and Hawthorne lost his job as a result.<sup>392</sup> Hawthorne then sued OCB and Hameed in a state court under Oklahoma law for causing his job loss and emotional distress.<sup>393</sup> A jury ultimately awarded the Hawthorne, \$ 175,000 in compensatory damages.<sup>394</sup> On appeal, OCB challenged the state court’s jurisdiction over Hawthorne’s action because they claimed that it was based solely upon an alleged violation of the bankruptcy stay.<sup>395</sup>

The court first reasoned that “the bankruptcy court has the responsibility to determine the effects of its own stay and to enforce its own orders.....Any proceedings involving the bankrupt debtor are outside a state court’s jurisdiction.”<sup>396</sup> The court, however, acknowledged that it had not found any case involving a similar factual scenario.<sup>397</sup> The court found that OCB had a lawful right to garnish Hawthorne’s wages until he filed for bankruptcy.<sup>398</sup> The court explained that OCB’s acts “became ‘wrongful’ or ‘negligent’ only under federal law upon the

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<sup>388</sup> Daniel W. Hawthorne v. Akhtar Hameed, 836 P.2d 683 (Okla. Ct. App. 1989).

<sup>389</sup> See *id.* at 684.

<sup>390</sup> See *id.*

<sup>391</sup> *Id.*

<sup>392</sup> *Id.*

<sup>393</sup> *Id.*

<sup>394</sup> *Id.* at 685..

<sup>395</sup> *Id.*

<sup>396</sup> *Id.* at 685. (citing Barber-Greene Co. v. Zeco Co., 17 B.R. 248 (Bankr. D. Minn. 1982)).

<sup>397</sup> See *id.*

<sup>398</sup> *Id.* at 686.

imposition of the automatic stay.”<sup>399</sup> Thus, the court reasoned that OCB’s alleged wrongful garnishment was not actionable under state law because Hawthorne was not entitled to relief in state court for acts arising solely from a violation of the automatic stay ordered by the federal bankruptcy court.”<sup>400</sup> Accordingly, the court held that state court lacked jurisdiction over Hawthorne’s action, concluding: “This matter should have been brought before the bankruptcy court for violation of its own order. This was the exclusive province of the bankruptcy court.”<sup>401</sup>

## 2. *Halas v. Platek*.<sup>402</sup>

Another jurisdictional issue was raised in *Halas v. Platek*,<sup>403</sup> where the court held that only bankruptcy courts have jurisdiction to impose sanctions for violating the stay.<sup>404</sup> In that case, a state court lawsuit had been instigated against the debtor a few days pre-petition.<sup>405</sup> The debtor was allegedly unaware of this court action when he filed Chapter 13 petition.<sup>406</sup> While the stay was in effect, the state court rendered a default judgment against the debtor.<sup>407</sup> Approximately a month afterwards, the debtor informed the plaintiff’s attorney of the bankruptcy, apparently for the first time.<sup>408</sup> The debtor’s bankruptcy case was dismissed and closed a few months later.<sup>409</sup>

The plaintiff’s attorney in the state court action subsequently transferred the file to a second attorney to enforce the judgment, and the second attorney caused the debtor’s wages to be

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<sup>399</sup> *Id.*

<sup>400</sup> *Id.*

<sup>401</sup> *Id.*

<sup>402</sup> *Halas v. Platek*, 239 B.R. 784 (N.D. Ill. 1999).

<sup>403</sup> *Id.*

<sup>404</sup> *See id.* at 792.

<sup>405</sup> *See id.* at 786.

<sup>406</sup> *Id.*

<sup>407</sup> *Id.*

<sup>408</sup> *Id.*

<sup>409</sup> *See id.* at 787.

garnished.<sup>410</sup> Roughly a year after the bankruptcy court had dismissed his Chapter 13 case, the debtor moved the state court to set aside the default judgment on the ground that the judgment had been rendered in violation of the stay, i.e., the state court had lacked subject matter jurisdiction.<sup>411</sup> The debtor requested the return of the monies collected and any other relief that the state court might deem just.<sup>412</sup> The state court vacated its order.<sup>413</sup> The state court believed that it had jurisdiction to decide that the stay had applied to the action that had been before it, although this jurisdictional issue was apparently not raised.<sup>414</sup> The state court, however, denied any further relief and ordered the debtor to pay the fees of the two attorneys.<sup>415</sup>

The debtor then returned to the bankruptcy court seeking sanctions against the two attorneys under 11 U.S.C. § 362(h) for willfully violating the stay.<sup>416</sup> The bankruptcy court reopened the case for the limited purpose of considering the Section 362(h) claim and then denied the debtor's motion on res judicata grounds.<sup>417</sup> The debtor had sought equivalent relief in the state tribunal, praying not only for the returns of the monies collected, but also for any other relief that the state court might deem just and equitable.<sup>418</sup> In other words, the debtor had asked the state court, in effect, to impose sanctions for violating the stay.<sup>419</sup> Having failed to obtain all that he wanted in the state forum, the debtor was precluded from relitigating his claim in the bankruptcy court.

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<sup>410</sup> *Id.*

<sup>411</sup> *Id.*

<sup>412</sup> *Id.*

<sup>413</sup> Young, *supra* note 108, at 66.

<sup>414</sup> *Id.*

<sup>415</sup> *Id.*

<sup>416</sup> *Id.*

<sup>417</sup> *Id.*

<sup>418</sup> *Id.*

<sup>419</sup> *See* Young, *supra* note 108, at 66.

On appeal, the district court reversed, holding that the state court had no jurisdiction to impose sanctions for violating the stay.<sup>420</sup> Therefore, regardless of whether this defense had actually been alleged, the state court judgment could have no res judicata effect in a Section 362(h) proceeding before the bankruptcy court.<sup>421</sup>

The *Halas*<sup>422</sup> district court pointed out that there was a dearth of legislative history concerning 11 U.S.C. § 362(h).<sup>423</sup> The one court of appeals to address the issue had suggested that bankruptcy courts have exclusive jurisdiction to impose sanctions for a stay violation under 11 U.S.C. § 362(h).<sup>424</sup> As the district court in *Halas*<sup>425</sup> correctly perceived, however, the Seventh Circuit's statements in *Martin- Trigona v. Champion Fed. Sav. & Loan Ass'n*,<sup>426</sup> were only dicta, and, moreover, the Seventh Circuit may have confused 28 U.S.C. § 1334(a), which grants bankruptcy courts original and exclusive jurisdiction over bankruptcy cases, with 28 U.S.C. § 1334(b), which grants bankruptcy courts original, but not exclusive jurisdiction over proceedings arising in or under the Bankruptcy Code, and over proceedings related to a bankruptcy case.<sup>427</sup>

The *Halas*<sup>428</sup> district court observed that a few state courts had addressed the issue.<sup>429</sup> Of the two that had discussed the matter at greatest lengths, the *Hawthorne*<sup>430</sup> court had concluded that bankruptcy courts alone have jurisdiction to impose sanctions for a stay violation, while the *Powell*,<sup>431</sup> court had decided that 11 U.S.C. § 362(h) creates a federal cause of action, but that

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<sup>420</sup> *Id.* at 67.

<sup>421</sup> *Id.*

<sup>422</sup> *See Halas*, 239 B.R. 784 (N.D. Ill. 1999).

<sup>423</sup> Young, *supra* note 108, at 67; *See also* Price v. Rochford, 947 F.2d 829 (7<sup>th</sup> Cir. 1991); Pettitt v. Baker, 876 F.2d 456 (5<sup>th</sup> Cir. 1989).

<sup>424</sup> Young, *supra* note 108, at 67; *See Martin-Trigona v. Champion Fed. Sav. & Loan Ass'n*, 892 F.2d 575 (7<sup>th</sup> Cir. 1989).

<sup>425</sup> *Halas*, 239 B.R. 784 (N.D. Ill. 1999).

<sup>426</sup> *Martin- Trigona*, 892 F.2d 575 (7<sup>th</sup> Cir. 1989).

<sup>427</sup> Young, *supra* note 108, at 67.

<sup>428</sup> *Halas*, 239 B.R. 784 9N.D. Ill. 1999).

<sup>429</sup> *Id.* at 789.

<sup>430</sup> *Hawthorne*, 836 P.2d 683, 686 (Okla. Ct. App. 1989).

<sup>431</sup> *Powell*, 684 A.2d 769 (D.C. 1995).

such an action may be prosecuted in a state as well as a bankruptcy court.<sup>432</sup> Ultimately, the *Halas*<sup>433</sup> district court found the reasoning in *Hawthorne*<sup>434</sup> more persuasive.<sup>435</sup>

The *Halas*<sup>436</sup> district court was correct in holding that only bankruptcy courts have jurisdiction to impose sanctions for stay violations, whether under Section 362(h) or otherwise.<sup>437</sup> In reaching this conclusion, however, the district court relied on two related and complementary, but nonetheless distinct lines of authority and reasoning, seemingly without realizing the difference.<sup>438</sup> On the one hand, exclusive jurisdiction over stay violations is essential to protect the bankruptcy court's exclusive jurisdiction over the bankruptcy estate and its property.<sup>439</sup> On the other, the automatic stay is equivalent to an order of the bankruptcy court, and it has long been settled that only the court whose authority had been violated, has jurisdiction to impose sanctions on the offending party.<sup>440</sup>

Analysis supporting the view that bankruptcy courts have exclusive jurisdiction to impose sanctions for violation of the automatic stay:

1. **Bankruptcy court's exclusive control over the case and the property of the estate**

A bankruptcy court has exclusive jurisdiction over the bankruptcy case as per 28 U.S.C. § 1334(a).<sup>441</sup> It also has exclusive jurisdiction over the property of the debtor as per 28 U.S.C. § 1334(e).<sup>442</sup> The automatic stay functions to preserve and enforce that exclusive jurisdiction and

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<sup>432</sup> Young, *supra* note 108, at 67.

<sup>433</sup> *Halas*, 239 B.R. 784 (N.D. Ill. 1999).

<sup>434</sup> *Hawthorne*, 836 P.2d 683.

<sup>435</sup> See Young, *supra* note 108, at 67.

<sup>436</sup> *Hawthorne*, 836 P.2d at 686.

<sup>437</sup> Young, *supra* note 109, at 68.

<sup>438</sup> *Id.*

<sup>439</sup> *Id.*

<sup>440</sup> *Id.*

<sup>441</sup> See *infra* note 253.

<sup>442</sup> See 28 U.S.C. § 133(e)(1994).

to bring all claims under the oversight of one forum.<sup>443</sup> The strong implication is that bankruptcy courts must have exclusive jurisdiction to enforce the stay through sanctions in order to maintain its exclusive jurisdiction over the case and over the estate property.<sup>444</sup> This appears to be the reasoning behind the dicta in *Martin- Trigona*<sup>445</sup>, which the *Halas*<sup>446</sup> district court cited.<sup>447</sup> Several state courts have either held or opined that bankruptcy courts have exclusive jurisdiction over proceedings under 11 U.S.C. § 362(h) on these grounds.<sup>448</sup>

A number of decisions of the federal court seem to support this view. In *Gonzales v. Parks*,<sup>449</sup> the Ninth Circuit held that a state court was without jurisdiction to entertain a creditor's claim that the debtor's filing of a bankruptcy petition constituted an abuse of process.<sup>450</sup> Such a proceeding would amount to a collateral attack on the petition itself and undermine the bankruptcy court's exclusive jurisdiction over the case.<sup>451</sup> The *Gonzales*<sup>452</sup> court stated, "A congressional grant of exclusive jurisdiction to the federal courts includes the implied power to protect that grant."<sup>453</sup> Following *Gonzales*,<sup>454</sup> the court in *Koffman v. Ostioimplant Technology, Inc.*,<sup>455</sup> held that a corporation against which an involuntary Chapter 7 petition had been filed could not maintain state law claims against an offending creditor either for filing an improper petition or for allegedly violating the automatic stay.<sup>456</sup> Because of exclusive federal control

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<sup>443</sup> *In re Rimsat, Ltd.*, 98 F.3d 956 (7<sup>th</sup> Cir. 1996); *In re Way*, 229 B.R. 11 (9<sup>th</sup> Cir. B.A.P. 1998).

<sup>444</sup> Young, *supra* note 108, at 69.

<sup>445</sup> *Martin- Trigona*, 892 F.2d 575.

<sup>446</sup> *Halas*, 239 B.R. 784.

<sup>447</sup> *See id.*

<sup>448</sup> *Labat v. Bank of Coweta*, 460 S.E. 2d 831 (Ga. Ct. App. 1995); *Pemstein v. Stimpson*, 630 N.E.2d 608 (Mass. App. Ct. 1994).

<sup>449</sup> *Gonzales v. Parks*, 830 F.2d 1033 (9<sup>th</sup> Cir. 1987).

<sup>450</sup> Young, *supra* note 108, at 69.

<sup>451</sup> *Id.*; *See Cf. Donovan v. City of Dallas*, 377 U.S. 408 (1964) (state courts may not enjoin proceedings in federal courts).

<sup>452</sup> *Gonzales*, 830 F.2d 1033.

<sup>453</sup> *Id.* at 1036.

<sup>454</sup> *Id.*

<sup>455</sup> *Koffman v. Ostioimplant Technology, Inc.*, 182 B.R. 115 (D. Md. 1995)

<sup>456</sup> Young, *supra* note 108, at 69.

over bankruptcy, remedies had to be provided solely by federal law.<sup>457</sup> The Sixth Circuit, in *Accord Pertuso v. Ford Motor Credit Co.*,<sup>458</sup> held that there is no state law cause of action for violating the stay; federal law preempts any state law in this regard.<sup>459</sup> Moreover, federal courts must have exclusive jurisdiction over stay violations in order to maintain uniformity.<sup>460</sup>

2. **Only the court whose authority has been violated or disobeyed can impose sanctions for such a violation or disobedience**

At a broader level, it has long been settled that only the court whose authority has been flouted may impose sanctions for the violation, particularly by way of civil contempt proceedings.<sup>461</sup> Jurisdiction to sanction by way of civil contempt or any analogous method rests exclusively with the court whose authority was ignored or whose orders were violated.<sup>462</sup>

The automatic stay is not an “order” of the bankruptcy court.<sup>463</sup> The stay takes effect by operation of law; an affirmative act by the bankruptcy court is required to lift or modify the stay.<sup>464</sup> Nonetheless, the stay is usually treated as equivalent to a bankruptcy court injunction, and certainly only the bankruptcy court in which the case is pending has original jurisdiction to grant relief from the stay.<sup>465</sup> The *Gruntz*<sup>466</sup> court stated: “The automatic stay is an injunction issuing from the authority of the bankruptcy court, and bankruptcy court orders are not subject to collateral attacks in other courts.”<sup>467</sup>

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<sup>457</sup> *Id.*

<sup>458</sup> *Accord Pertuso v. Ford Motor Credit Co.*, 233 F.3d 417 (6<sup>th</sup> Cir. 2000)

<sup>459</sup> Young, *supra* note 108, at 70.

<sup>460</sup> *Id.*

<sup>461</sup> *Id.*; *See Ex parte Bradley*, 74 U.S. (7 Wall) 364 (1868); *U.S. v. Barnett*, 330 F.2d 369 (5<sup>th</sup> Cir. 1963) (en banc), certified question answered, 376 U.S. 681 (1964)..

<sup>462</sup> Young, *supra* note 108, at 72.

<sup>463</sup> *Id.*

<sup>464</sup> *Id.*; *See Cf. In re Schimmelpennicck*, 183 F.3d 347 (5<sup>th</sup> Cir. 1999) (contrasting an ancillary proceeding under 11 U.S.C. § 304 with an ordinary bankruptcy case in this respect).

<sup>465</sup> Young, *supra* note 108, at 72.

<sup>466</sup> *Gruntz I*, 202 F.3d 1074 (9<sup>th</sup> Cir. 2000) (en banc)

<sup>467</sup> *Id.* at 1082.

11 U.S.C. § 362(h) was enacted in 1984 in order to make it easier for an aggrieved debtor to recover for a stay violation; the standards governing a claim under Section 362(h) are not as strict as in a proceeding under Section 105(a).<sup>468</sup> For one thing, clear and convincing evidence is required in a civil contempt proceeding whereas most courts hold that the standard proof under Section 362(h) is merely preponderance of evidence.<sup>469</sup> Moreover, some courts require proof of bad faith before they will impose sanctions under Section 105(a).<sup>470</sup> There is another difference as well. Although a debtor or any aggrieved party with standing may seek sanction under Section 105(a), there is a split of authority as to who may invoke Section 362(h).<sup>471</sup> The great weight of authority, however, holds that Section 362(h) speaks of an “individual” aggrieved by a stay violation, and that this term refers only to a natural person.<sup>472</sup> Corporate debtors or other entities that are not natural persons must seek to vindicate their rights under 11 U.S.C. § 105(a) if the stay is violated.<sup>473</sup>

Although a proceeding to obtain sanctions under Section 362(h) may differ from a proceeding under Section 105(a), the two serve similar objectives, and both are functionally equivalent to civil contempt actions for violating the automatic stay, which is treated as a court order for relevant purposes.<sup>474</sup> Indeed, there is nothing to prevent an individual debtor from seeking to vindicate his or her rights under both statutes.<sup>475</sup> Once this is understood, the principles laid down in *Ex parte Bradley*<sup>476</sup> and *Gray v. Petoseed Co., Inc.*,<sup>477</sup> immediately come

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<sup>468</sup> Young, *supra* note 108, at 72;

<sup>469</sup> *Id.*; see also *In re Florio*, 229 B.R. 606 (S.D.N.Y. 1999); *Hanna Coal Co. v. I.R.S.*, 218 B.R. 825 (W.D. Va. 1997); *In re Pincombe*, 256 B.R. 774 (Bankr. N.D. Ill. 2000).

<sup>470</sup> See *Shaddock v. Rodolakis*, 221 B.R. 573 (D. Mass. 1998).

<sup>471</sup> *Id.*

<sup>472</sup> *Id.*

<sup>473</sup> *Id.*

<sup>474</sup> *Id.*; see also *A & J Auto Sales, Inc.*, 223 B.R. 839 (Bankr. D.N.H. 1998).

<sup>475</sup> Young, *supra* note 108, at 74.

<sup>476</sup> *Ex parte Bradley*, 74 U.S. (7 Wall.) 364.

<sup>477</sup> *Gray*, 985 F. Supp. 625.

into play.<sup>478</sup> A state court has no more authority to entertain an action under 11 U.S.C. § 105(a), which clearly applies only in bankruptcy courts.<sup>479</sup> A state court simply has no jurisdiction to vindicate the dignity or authority of a bankruptcy court, no matter what theory may be used.<sup>480</sup> The best reasoned state court decisions have adopted this position.<sup>481</sup> The *Hawthorne*<sup>482</sup> court stated: “The bankruptcy court has the power to control its own proceedings and to punish for contempt any violations of Section 362.....The bankruptcy court has the responsibility to determine the effects of its own stay and to enforce its own orders....Similarly, in Oklahoma, the power of a state court to punish for contempt lies exclusively in the court whose order was violated.”<sup>483</sup> Likewise the court in *Ramdharry v. Gurrer*<sup>484</sup> succinctly held: “This is a matter which should be determined by the Bankruptcy Court, not the state court. An award of monetary damages under Section 362(h) for a violation of a court order is rightfully within the jurisdiction of the Court whose order was violated.”<sup>485</sup>

The *Halas*<sup>486</sup> court cited both *Hawthorne*<sup>487</sup> and *Ramdharry*<sup>488</sup> with approval and placed particular reliance on *Hawthorne*.<sup>489</sup> This line of cases focusing on a court’s exclusive jurisdiction to impose sanctions for violations of its own orders and to vindicate the integrity of its own proceedings ultimately provides the strongest support for the district court’s decision in *Halas*.<sup>490</sup> The exclusive jurisdiction of any court to impose civil penalties for violation of its

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<sup>478</sup> Young, *supra* note 108, at 74.

<sup>479</sup> *Id.*

<sup>480</sup> *Id.*

<sup>481</sup> See *Hawthorne*, 836 P.2d 683.

<sup>482</sup> *Id.*

<sup>483</sup> See *Hawthorne*, 836 P.2d at 685.

<sup>484</sup> *Ramdharry v. Gurrer*, No. CV 89 42620 S, 1995 WL 41353 (Conn. Super. Ct. Jan. 25, 1995)

<sup>485</sup> *Id.*

<sup>486</sup> *Halas*, 239 B.R. at 784.

<sup>487</sup> See *Hawthorne*, 836 P.2d at 685.

<sup>488</sup> *Gurrer*, No. CV 89 42620 S, 1995 WL 41353

<sup>489</sup> *Hawthorne*, 836 P.2d at 685; See Young, *supra* note 107, at 75.

<sup>490</sup> Young, *supra* note 108, at 75.

own authority leads to the conclusion that only bankruptcy court may impose sanctions for a stay violation, whether under 11 U.S.C. § 362(h) or 11 U.S.C. § 105(a).<sup>491</sup>

**(c) Issues Pertaining To The Repossession Of The Debtor’s Property (By The Creditor) Before Filing Of The Bankruptcy Petition-**

Another type of automatic stay dispute has arisen particularly in the context of consumer bankruptcies.<sup>492</sup> A matter related to this that has continued to generate controversy is whether a creditor that has lawfully repossessed a debtor’s property *before* the filing of a bankruptcy petition (pre-petition), violates the automatic stay by simply retaining possession of that property *after* the automatic stay comes into effect, until adequate protection is offered.<sup>493</sup>

In *In re Diamond Indus. Corp.*,<sup>494</sup> there was a split of authority as to whether merely retaining possession amounts to “exercising control” for purposes of 11 U.S.C. § 362(a)(3).<sup>495</sup> Section 362(a)(3) provides that any act to obtain property of the estate is expressly subject to the automatic stay.<sup>496</sup>

“Under existing law, it may be unclear whether a creditor in rightful possession of a debtor’s property at the outset of a bankruptcy case must return the property in the absence of adequate protection.”<sup>497</sup> Some courts have held that the creditor has an absolute duty to turn over the property regardless of adequate protection, and hence that the creditor violates the

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<sup>491</sup> *Id.*

<sup>492</sup> Thomas E. Plank, *The Creditor In Possession Under the Bankruptcy Code: History, Text, and Policy*, 59 MD. L. REV. 253 (2000).

<sup>493</sup> Young, *supra* note 108, at 100.

<sup>494</sup> *In re Diamond Indus. Corp.*, 265 B.R. 707 (Bankr. E.D. Va. 1999).

<sup>495</sup> *Id.* at 712-714.

<sup>496</sup> *See* 11 U.S.C. § 362(a)(3).

<sup>497</sup> Hon. Eugene R. Wedoff, *An Updated Analysis of the Consumer Bankruptcy Provisions of H.R. 833 Bankruptcy Reform Act of 1999*, As Passed by the House of Representatives, 31 (Nov. 1, 1999). [www.abiworld.org](http://www.abiworld.org)

automatic stay if this is not done.<sup>498</sup> Others have held that merely retaining the property does not violate the stay and that the creditor has no duty to surrender the property until adequate protection is given.<sup>499</sup>

There are at least four instances in which such disputes might not arise.<sup>500</sup> First, if the debtor had lost all rights in the property pre-petition, the repossessing creditor would not violate the stay by retaining or disposing of the property after the bankruptcy petition is filed (post-petition).<sup>501</sup> For example, if the debtor had been leasing a vehicle under a contract that was a true lease and not a disguised security arrangement, and if the debtor had defaulted and the lessor had taken possession of the vehicle, and if there were no contractual or statutory right for the debtor lessee to cure his or her default after repossession, then the debtor lessee would have lost all rights in the property.<sup>502</sup> In that case, the lessor would not violate the stay by retaining or selling the item post-petition.<sup>503</sup>

Second, and conversely, if the secured creditor has lawfully repossessed the property before the petition, but if the debtor still has rights in the property when the petition is filed, such as legal title and/or a right of redemption, then the bankruptcy estate would succeed to the debtor's rights under 11 U.S.C. § 541(a).<sup>504</sup> In that case, there would be no disagreement that the

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<sup>498</sup> See *In re Bunton*, 246 B.R. 851 (Bankr. N.D. Ohio 2000); *Brooks*, 207 B.R. 738.; *In re Sharon*, 200 B.R. 181 (Bankr. S.D. Ohio 1996), aff'd, 234 B.R. 676 (6<sup>th</sup> Cir. B.A.P. 1999).

<sup>499</sup> See *In re Spears*, 223 B.R. 159 (Bankr. N.D. Ill. 1998); *In re Fitch*, 217 B.R. 286 (Bankr. S.D. Cal. 1998); *In re Deiss*, 166 B.R. 92 (Bankr. S.D. Tex. 1994).

<sup>500</sup> Young, *supra* note 108, at 101.

<sup>501</sup> *Id.*

<sup>502</sup> *Id.*

<sup>503</sup> *Id.* See *In re Lamar*, 249 B.R. 822 (Bankr. S.D. Ga. 2000) But see *In re Dash*, 267 B.R. 815 (Bankr. D.N.J. 2001) (where lessor had repossessed motor vehicle pre-petition without giving notice of termination, lease remained in force and could be assumed or rejected; debtor's leasehold interest was estate property).

<sup>504</sup> Young, *supra* note 108, at 102; see *In re Coleman*, 229 B.R. 428 (Bankr. N.D. Ill. 1999).

creditor would violate the stay if it sold the property or otherwise purported to cut off the debtor's rights without first obtaining relief from the stay.<sup>505</sup>

Third, a creditor does not violate the stay if there is a specific statutory exception.<sup>506</sup> For example, if a debtor has been unable to pay for repairs to a vehicle, if applicable state law allows for a possessory artisan's lien, and if the creditor has lawfully retained possession before the filing of the bankruptcy petition, pursuant to the artisan's lien statute, then 11 U.S.C. § 362(b)(3)<sup>507</sup> shields the creditor if it continues to retain the vehicle post-petition and to assert its rights under the lien.<sup>508</sup>

Fourth, in *In re U.S. Physicians, Inc.*,<sup>509</sup> the court held that a creditor that has wrongfully repossessed the property pre-petition, does not violate the stay by refusing to return the property post-petition.<sup>510</sup> In such a case, the estate acquires the debtor's right to maintain an action for replevin, conversion, trespass to chattels, or breach of the underlying contract, but the estate does not necessarily automatically acquire property itself.<sup>511</sup> The rationale is that a refusal to undo a pre-petition wrong, without more, is not a violation of the stay.<sup>512</sup>

The real dispute is over whether a creditor who has lawfully repossessed the debtor's property pre-petition must turn the property over post-petition, even without adequate protection, and whether the creditor violates the stay by simply retaining the property until adequate protection is granted.<sup>513</sup> The Eleventh Circuit, in *In re Lewis*<sup>514</sup> has held that, under Alabama law, a default terminates all of the debtor's rights under a secured installment sale

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<sup>505</sup> Young, *supra* note 108, at 101.

<sup>506</sup> *Id.*

<sup>507</sup> See *infra* note 85.

<sup>508</sup> Young, *supra* note 108, at 103.

<sup>509</sup> *In re U.S. Physicians, Inc.*, 235 B.R. 267 (Bankr. E.D. Pa. 1999).

<sup>510</sup> *Id.* at 267-268.

<sup>511</sup> *Id.*

<sup>512</sup> Young, *supra* note 108, at 103.

<sup>513</sup> See Robert M. Lloyd, *Lender Liability for Wrongful Repossession*, 114 BANKING L.G. 612 (1997).

<sup>514</sup> *In re Lewis*, 137 F.3d 1280 (11<sup>th</sup> Cir. 1998).

contract.<sup>515</sup> The debtor no longer has any rights in the collateral.<sup>516</sup> Thus, according to the Eleventh Circuit, a creditor that had lawfully taken possession before the filing of the bankruptcy petition would not violate the stay by refusing to turn over the property post-petition.<sup>517</sup>

However, a district court in Florida has held that, under Florida law, title to a vehicle passes upon default and possession.<sup>518</sup> Thus, even if the debtor retains a right of redemption, this, without more, is not sufficient to make the vehicle estate property, and a creditor, therefore, would not violate the stay by retaining the vehicle.<sup>519</sup> The bankruptcy courts in *In re Regan*<sup>520</sup> has followed this decision while the courts in *In re Shannarah*<sup>521</sup> and in *In re Baker*<sup>522</sup> have rejected it.<sup>523</sup>

Typically, the dispute over whether a creditor who has lawfully repossessed property pre-petition must turn the property over post-petition, (even without the grant of adequate protection), and whether the creditor violates the stay by simply retaining the property until adequate protection is granted, arises in consumer cases, and normally the repossessed property is a motor vehicle.<sup>524</sup> Often, the adequate protection controversy involves whether the debtor must maintain insurance on the vehicle, in addition to whether the debtor must make payments to the secured creditor, before the creditor is required to return the property.<sup>525</sup>

Many courts, perhaps a majority, have held that the repossessing secured creditor must turn over the property upon demand, even without adequate protection, if the debtor still holds

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<sup>515</sup> *See id.* at 1283.

<sup>516</sup> *Id.*

<sup>517</sup> *See id.* at 1280.

<sup>518</sup> *See In re Kalter*, 257 B.R. 93 (M.D. Fla. 2000).

<sup>519</sup> *Id.*

<sup>520</sup> *In re Regan*, 264 B.R. 776 (Bankr. S.D. Fla. 2001).

<sup>521</sup> *In re Shannarah*, 268 B.R. 657 (Bankr. M.D. Fla. 2001).

<sup>522</sup> *In re Baker*, 264 B.R. 759 (Bankr. M.D. Fla. 2001).

<sup>523</sup> Young, *supra* note 108, at 102.

<sup>524</sup> *See Lloyd*, *supra* note 513.

<sup>525</sup> *Id.*

legal title and if there is still a right to cure.<sup>526</sup> If the creditor fails to do so, the creditor will be in violation of the stay.<sup>527</sup>

A discussion of some of the relevant cases in this regard follows:

1. *In re Knaus*<sup>528</sup>

In this case, which was brought before the Court of Appeals for the Eighth Circuit, the Appellant had argued that the Appellee had violated the automatic stay imposed by 11 U.S.C. § 362 when it failed, upon Appellant's filing for bankruptcy, to voluntarily turn over grain and equipment it had previously taken from the appellant.<sup>529</sup> Appellee had argued that it had no obligation to turn over property, because it had taken the property before the petition was filed and the stay imposed.<sup>530</sup> The bankruptcy court had held that the creditor violated the automatic stay of section 362 of the code, 11 U.S.C. § 362, by not voluntarily returning the property after the filing of the bankruptcy petition.<sup>531</sup> On appeal, the district court, however, held that the failure to voluntarily turn over property taken lawfully before the filing of the bankruptcy petition was not a violation of the automatic stay provisions.<sup>532</sup>

The Eighth Circuit, reversed the judgment, holding that Appellee's failure, upon Appellant's filing for bankruptcy, to voluntarily turn over property taken before the filing of the bankruptcy petition violated the stay.<sup>533</sup> The court held that Appellant was entitled to punitive damages because Appellee's conduct was willful and egregious.<sup>534</sup> The court stated that it failed

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<sup>526</sup> See *Bunton*, 246 B.R. 851; *Brooks*, 207 B.R. 738; *Sharon*, 200 B.R. 181.

<sup>527</sup> See *id.*

<sup>528</sup> *In re Knaus*, 889 F.2d 773 (8<sup>th</sup> Cir. 1989).

<sup>529</sup> *Id.*

<sup>530</sup> *Id.*

<sup>531</sup> *Id.* at 774.

<sup>532</sup> *Knaus*, 889 F.2d at 774.

<sup>533</sup> *Id.*

<sup>534</sup> See *id.* at 775.

to see any distinction between a failure to return property taken before the stay and a failure to return the property taken after the stay.<sup>535</sup> In both cases, the law clearly required turnover.<sup>536</sup>

The Supreme Court in *United States v. Whiting Pools, Inc*<sup>537</sup> had made a distinction in this regard, in that property seized, but not yet sold before the filing of the bankruptcy petition was the property of the estate, subject to turnover requirements of section 542.<sup>538</sup> The Eighth Circuit argued that the duty to turn over the property was not contingent upon any predicate violation of the stay, any order of the bankruptcy court, or any demand by the creditor.<sup>539</sup> Rather, the duty would arise upon the filing of the bankruptcy petition.<sup>540</sup> The court held that the failure to fulfill that duty, regardless of whether the original seizure was lawful, constituted a prohibited attempt to “exercise control over the property of the estate” in violation of the automatic stay.<sup>541</sup>

The court cited late Chief Bankruptcy Judge Stewart’s opinion on remand: “ The principle is simply this: that a person holding property of a debtor who files bankruptcy proceedings becomes obligated, upon discovering the existence of the bankruptcy proceedings, to return that property to the debtor (in chapter 11 or chapter 13 proceedings) or his trustee (in chapter 7 proceedings). Otherwise, persons who could make no substantial claim to a debtor’s property in their possession could, without costs to themselves, compel the debtor or his trustee to bring suit as a prerequisite to returning the property, the powers of a bankruptcy court and its officers to collect the estate for the benefit of creditors would be vastly reduced. The general creditors, for

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<sup>535</sup> *Id.*

<sup>536</sup> *Id.*

<sup>537</sup> *United States v. Whiting Pools, Inc.*, 462 U.S. 198 (1983).

<sup>538</sup> *Knaus*, 889 F.2d at 775 (citing *Whiting Pools*, 462 U.S. 198).

<sup>539</sup> *See id.*

<sup>540</sup> *Id.*

<sup>541</sup> *Id.*

whose benefit the return of property is sought, would have needlessly to bear the cost of its return. And those who unjustly retain possession of such property might do so with impunity.”<sup>542</sup>

2. **In re Brooks**<sup>543</sup>

In this case, the dealership had repossessed the debtors’ car on June 20, 1996.<sup>544</sup> On June 20, 1996, the debtors filed for Chapter 13 bankruptcy and started an adversary proceeding seeking turnover of the car.<sup>545</sup> That day, their attorney requested the dealership to return the car.<sup>546</sup> The dealership demanded proof of insurance, which was provided on June 28, 1996.<sup>547</sup> The dealership told the debtors that they could pick up the car from a lot about 40 miles away, but the lot closed for the weekend.<sup>548</sup> The debtors had their car towed back and rented a car while the dealership was in possession.<sup>549</sup> Granting the motion in part, the court explained that the unsecured creditors should not have been called to pay the cost of transporting the vehicle back to the debtor.<sup>550</sup> By making the car available in 40 miles away, the dealership failed to fulfill its responsibility of returning the car to the debtors’ possession.<sup>551</sup> The court held the response time unreasonable, and three days would have been reasonable.<sup>552</sup>

The court noted that the dealership’s duty was not dependent on proof of insurance.<sup>553</sup> The court found a willful violation, requiring an award of costs.<sup>554</sup> However, finding no egregious conduct, the court awarded no punitive damages.<sup>555</sup>

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<sup>542</sup> *Knaus*, 889 F.2d at 775.

<sup>543</sup> *Brooks*, 207 B.R. 738 (Bankr. N.D. Fla. 1997).

<sup>544</sup> *Id.*

<sup>545</sup> *Id.*

<sup>546</sup> *Id.*

<sup>547</sup> *Id.*

<sup>548</sup> *Id.*

<sup>549</sup> *Id.*

<sup>550</sup> *Id.*

<sup>551</sup> *Id.* at 738.

<sup>552</sup> *Id.*

<sup>553</sup> *Id.*

<sup>554</sup> *Id.* at 738-39.

<sup>555</sup> *Id.*

In arriving at its conclusion, the court stated: “[T]he filing of a bankruptcy petition imposes automatically a stay upon most actions by creditors to satisfy their claims against the debtor (11 U.S.C. § 362(a)(3)). Section 542 provides that an entity, including a secured creditor, who possesses property of the debtor at the time the debtor files a bankruptcy petition shall deliver to the trustee, an account, for such property or the value of such property, unless such property is of inconsequential value or benefit to the estate.”<sup>556</sup> However, the court did not explain as to what kind of property could be considered inconsequential. The court further held that the collateral should be returned to the locale of repossession.<sup>557</sup> The court noted the bankruptcy court’s holding in *In re Belcher*,<sup>558</sup> where the creditors had repossessed the vehicle not knowing that the debtor had filed for bankruptcy.<sup>559</sup> The *Belcher*<sup>560</sup> court held that although the repossession occurred from the debtor’s failure to notify the creditor of the bankruptcy filing, the creditor had a duty to return the vehicle to the place from where it was taken.<sup>561</sup>

Following are a few cases in which the courts have held that the creditor does not violate the stay by merely retaining possession of any vehicle or other property, and that the creditor is under no obligation to turn over the property unless and until the court so orders and adequate protection is provided:

1. ***In re Fitch***<sup>562</sup>

The debtor, in this case, had purchased a car on credit and defaulted on the obligation.<sup>563</sup>

The secured creditor then repossessed the car.<sup>564</sup> The debtor then filed her Chapter 13

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<sup>556</sup> *Id.* at 740 (quoting Judge Lewis Killian, Jr.).

<sup>557</sup> *Id.*

<sup>558</sup> *In re Belcher*, 189 Bankr. 16 (Bankr. S.D. Fla., 1995).

<sup>559</sup> *See Brooks*, 207 B.R. at 741.

<sup>560</sup> *Belcher*, 189 Bankr. 16.

<sup>561</sup> *Belcher*, 189 Bankr. at 18.

<sup>562</sup> *In re Fitch*, 217 B.R. 286 (Bankr. S.D. Cal. 1998).

<sup>563</sup> *Id.*

<sup>564</sup> *Id.*

bankruptcy petition and demanded that the secured creditor return the car.<sup>565</sup> The secured creditor refused to return the car absent showing of adequate protection in the form of insurance.<sup>566</sup> The debtor filed a motion for sanctions against the secured creditors for the retention of the car after receiving notice of the debtor's bankruptcy petition, which was denied.<sup>567</sup>

The court referred to several decisions<sup>568</sup> in the past determining that the secured creditor was not required to immediately turn over the car.<sup>569</sup> *In re Schwartz*<sup>570</sup> and in *In re Stringer*<sup>571</sup> the respective courts had held that only if the repossession takes place post-petition, it would violate the automatic stay and would, thus, be void and of no effect.<sup>572</sup> The *Fitch*<sup>573</sup> court, arrived at a similar conclusion stating that the repossession of the car was not a violation of the stay since it had occurred pre-petition.<sup>574</sup> According to 11 U.S.C. § 362(a)(3), the automatic stay prohibits, inter alia, any act “to exercise control over the property of the estate.”<sup>575</sup> The debtor, in this case, had argued that by retaining the car, the creditor violated subsection (a)(3) because retaining the car was an “act” to “exercise control over the property of the estate.”<sup>576</sup> The court, however, found that the right to possess the car was not property of the estate and thus, it did not find necessary to reach the issue of whether the retention of the car was an “act.”

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<sup>565</sup> *Id.*

<sup>566</sup> *Id.*

<sup>567</sup> *Id.*

<sup>568</sup> *See id.* at 288; (The court cited *Lewis*, 211 B.R. 970; *Matter of Brown*, 210 B.R. 878.882 (Bankr. S.D. Ga. 1997); *In re Massey*, 210 B.R. 693 (Bankr. Md. 1997).

<sup>569</sup> *Id.*

<sup>570</sup> *In re Schwartz*, 954 F.2d 569 (9<sup>th</sup> Cir. 1992).

<sup>571</sup> *In re Stringer*, 847 F.2d 549 (9<sup>th</sup> Cir. 1988).

<sup>572</sup> *Fitch*, 217 B.R. at 288.

<sup>573</sup> *Id.* at 286.

<sup>574</sup> *Id.* at 288.

<sup>575</sup> *See also* 11 U.S.C. § 362(a)(3)(1994).

<sup>576</sup> *Fitch*, 217 B.R. at 288.

In *In re Richardson*,<sup>577</sup> the court held that a violation of § 362(a)(3) required an affirmative act and that retention of a car repossessed pre-petition was not such an act.<sup>578</sup> The court, in holding that the right to possess the car was not property of the estate, argued that Section 541(a) of the Bankruptcy Code, which defines property, states that it includes “all legal or equitable interests of the debtor in property as of the commencement of the case.”<sup>579</sup> The court further explained that this provision was not intended to expand the debtor’s rights against others more than they existed at the commencement of the case, and thus whatever rights the debtor had in property at the commencement of the case, continued in bankruptcy, no more, no less.<sup>580</sup> The court stated that property rights were to be determined under state law,<sup>581</sup> and applying the relevant law of the state of California, the court determined that the right to possess the car was not among the property interests which became property of the estate; and thus creditors acts to exercise control over the right to possess the car did not violate the stay.<sup>582</sup> The court concluded that “[T]he car was and remained the property of the estate, and repossession did not change that. The right to possess the car, however, was transferred from the debtor to the creditor prior to the filing of the petition. Since the debtor did not have the unfettered right to possession at the time the petition was filed, the unfettered right to possession did not become property of the estate. Thus, the creditor’s refusal to return the car did not amount to a violation of the stay.”<sup>583</sup>

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<sup>577</sup> *In re Richardson*, 135 B.R. 256 (Bankr. E.D. Tex. 1992).

<sup>578</sup> *Fitch*, 217 B.R. at 289 (citing *id.* at 259).

<sup>579</sup> *Id.*

<sup>580</sup> *Id.*

<sup>581</sup> *Id.*

<sup>582</sup> *Id.*

<sup>583</sup> *Id.* at 291 (quoting Judge Peter Bowie)

3. *In re Spears*<sup>584</sup>

In this case, the debtor had purchased a vehicle under a retail installment contract and had financed it through the motor company.<sup>585</sup> The debtor failed to make any payments on the vehicle and the company repossessed it.<sup>586</sup> The debtor filed a Chapter 13 bankruptcy petition and sought for the return of the vehicle.<sup>587</sup> This case raised two issues: (i) First, in connection with the debtor's claim for return of the vehicle, the creditor argued that the debtor did not possess sufficient property interest in the vehicle, such that turn over could be ordered.<sup>588</sup> Second, the creditor contended that sanctions under § 362(h) were not required in the case as it had not violated the automatic stay in refusing to return the vehicle after receiving notice of the debtor's Chapter 13 filing.<sup>589</sup>

Citing *In re Johnson*,<sup>590</sup> this court noted that turn over was a remedy to obtain what was acknowledged to be property of the bankruptcy estate.<sup>591</sup> As a result of this, if the debtor did not have an interest in property at the commencement of the bankruptcy case, turnover could not be ordered.<sup>592</sup>

The *Spears*<sup>593</sup> court referenced the decision of the Supreme Court in *Whiting Pools*,<sup>594</sup> where the Court had determined that turnover could be ordered in cases where, prior to the commencement of reorganization proceedings, property of a Chapter 11 debtor had been

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<sup>584</sup> *In re Spears*, 223 B.R. 159 (Bankr. N.D. Ill. 1998)

<sup>585</sup> *Id.*

<sup>586</sup> *Id.*

<sup>587</sup> *Id.*

<sup>588</sup> *See id.* at 162.

<sup>589</sup> *Id.* at 62.

<sup>590</sup> *In re Johnson*, 215 B.R. 381 (Bankr. N.D. Ill. 1997).

<sup>591</sup> *Spears*, 223 B.R. at 162.

<sup>592</sup> *Id.*

<sup>593</sup> *Id.* at 159.

<sup>594</sup> *Whiting Pools*, 462 U.S. 198.

repossessed by a secured creditor.<sup>595</sup> Although an order under § 542(a) modifies a creditor's procedural rights available to protect and satisfy its lien, the Court reasoned that the creditor's rights under the Bankruptcy Code, including the right to adequate protection, replaced the protection afforded the creditor by its repossession remedy.<sup>596</sup> In addition, the *Whiting Pools*<sup>597</sup> decision had commented that a rehabilitation of a debtor's business was facilitated if property subject to creditors' security interests was included in the reorganization estate.<sup>598</sup> The Supreme Court noted that its analysis depended in part on the reorganization context before it, and the court left open the question whether § 542(a) would have the same broad effect in liquidation or adjustment of debt proceedings.<sup>599</sup> The *Spears*<sup>600</sup> court noted that under the Uniform Commercial Code ("UCC") as adopted in most states, after repossession, the debtor's interest in the vehicle is a right to redeem the vehicle.<sup>601</sup> The court distinguished its holding from the one in *Charles R. Hall Motors v, Inc v. Lewis*<sup>602</sup> by the Eleventh Circuit court in that *Lewis*<sup>603</sup> court had reached its result (under the law of Alabama) by finding that a right of redemption is not a sufficient property interest to warrant turnover of a repossessed vehicle.<sup>604</sup> The *Spears* court looked to Illinois law discussing the nature of a debtor's interest in a repossessed vehicle.<sup>605</sup> As under the Alabama cases, the Illinois Appellate Court had found that legal title to property

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<sup>595</sup> *See id.* at 206.

<sup>596</sup> *Id.*

<sup>597</sup> *Id.* at 198.

<sup>598</sup> *Id.* at 206-207.

<sup>599</sup> *Id.*

<sup>600</sup> *Spears*, 223 B.R. at 162.

<sup>601</sup> *Id.*

<sup>602</sup> *Charles R. Hall Motors, Inc. v. Lewis (In re Lewis)*, 137 F.3d 1280 (11<sup>th</sup> Cir. 1998).

<sup>603</sup> *Id.*

<sup>604</sup> *See Spears*, 223 B.R. at 164 (citing *Lewis*, 223 B.R. at 1284).

<sup>605</sup> *See id.*

subject to a security interest passes to a secured creditor after it takes possession following default.<sup>606</sup>

As to the question whether a creditor violated the stay by refusing to turn over a debtor's vehicle that is repossessed prior to the filing of a bankruptcy petition, the critical question before the court was whether turnover could be ordered before findings as to adequate protection were made.<sup>607</sup> The court referred to the bankruptcy court's decision in *In re Young*,<sup>608</sup> where the court stated that the passive act of continuing to possess property did not fall within the prohibition under § 362(h).<sup>609</sup> If a vehicle had been lawfully repossessed pre-petition, the creditor would have a right to possess the vehicle on the date the debtor filed for bankruptcy.<sup>610</sup> Since the purpose of the automatic stay is to maintain the status quo that existed on the date of a debtor's bankruptcy filing, the creditor should not have to turn over the vehicle absent assurance that its pre-petition position would be protected.<sup>611</sup> The decision in *Young*<sup>612</sup> commented that if § 362(a)(3) were interpreted as requiring immediate turnover, it would represent a dramatic shift from the pre-Code practice of allowing secured creditors to retain repossessed collateral until adequate protection was provided by the debtor.<sup>613</sup>

Importantly, too, it would contravene the statutory scheme under §§ 363(e) and 542(a) to find that a creditor has an affirmative duty to turn over collateral repossessed prior to bankruptcy.<sup>614</sup> Section 542(a) also limited turnover of property that could be used under §

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<sup>606</sup> *Id.*

<sup>607</sup> *Id.* at 165.

<sup>608</sup> *In re Young*, 193 B.R. 126.

<sup>609</sup> *Spears*, 223 B.R. at 165.

<sup>610</sup> *Id.*

<sup>611</sup> *See id.* at 165.

<sup>612</sup> *In re Young*, 193 B.R. 620 (Bankr. D.D.C. 1996)

<sup>613</sup> *See id.* at 166.

<sup>614</sup> *Id.*

363.<sup>615</sup> Under § 363(e) the creditor could obtain an order prohibiting a proposed use of the property unless the estate provided adequate protection.<sup>616</sup> This constituted a significant defense to the grant of a turnover order under § 542(a).<sup>617</sup> The defense would be abrogated by an interpretation of § 362(a)(3) requiring turnover without permitting invocation of the defense.<sup>618</sup> Such an approach would be contrary to the logical interaction of § § 363(e) and 542(a).<sup>619</sup> The burden would be on the trustee, when the issue would be raised, to prove adequate protection 11 U.S.C. § 363(o)(1).<sup>620</sup> Logically, therefore, the creditor should be entitled to hold onto the property during the pendency of the § 542 action until adequate protection question is resolved.<sup>621</sup> The obvious rationale implicit in permitting the secured creditor to retain possession of the seized property while opposing turnover under § 542(a) is that the creditor may suffer the very harm that adequate protection is designed to avoid if the property is turned over to the trustee before the trustee proves that the creditor is being given the adequate protection to which it is entitled.<sup>622</sup>

An excellent exposition of the competing points of view is given in the majority and the dissenting opinions in *In re Sharon*.<sup>623</sup> The majority espoused the position that a creditor who has repossessed pre-petition violates the stay by refusing to surrender the property, even if no adequate has been offered.<sup>624</sup> 11 U.S.C. § 363(a)(3) prohibits “any act to obtain possession of property of the estate or to exercise control over property of the estate” once a petition is filed.<sup>625</sup>

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<sup>615</sup> *Id.*

<sup>616</sup> *Id.*

<sup>617</sup> *Id.*

<sup>618</sup> *Id.*

<sup>619</sup> *Id.*

<sup>620</sup> *Id.*

<sup>621</sup> *Id.*

<sup>622</sup> *Id.*

<sup>623</sup> *In re Sharon*, 234 B.R. 676 (6<sup>th</sup> Cir. B.A.P. 1999).

<sup>624</sup> *See Young, supra* note 108, at 104-105.

<sup>625</sup> *See* 11 U.S.C. § 362(a)(3) (1994).

If, under applicable non-bankruptcy law, the debtor still holds legal title to the property or a right of redemption, the property becomes the property of the estate.<sup>626</sup> Anyone holding property as of the petition date is obliged to turn it over pursuant to § 542(a), even if the debtor would not necessarily have a right to immediate possession under non-bankruptcy law.<sup>627</sup> The *Sharon*<sup>628</sup> majority thus concluded that retaining possession of the repossessed property violates the stay.<sup>629</sup> There is nothing in 11 U.S.C. § 362(a)(3) that creates an exception to the stay if the creditor does not have adequate protection, and there is nothing in 11 U.S.C. § 542(a) that conditions turnover on adequate protection.<sup>630</sup> If a repossessing creditor wants adequate protection or relief from the stay, the creditor may seek it pursuant to 11 U.S.C. § 363(e) and/or § 362(f), but a creditor is not free to engage in self-help by retaining the property on its own initiative until adequate protection is provided, or by deciding by itself whether there is adequate protection.<sup>631</sup>

In a well argued dissent, Judge Stosberg expounded the competing view.<sup>632</sup> The stay is designed to freeze the status quo as of the petition date, and hence a mere passive retention of property lawfully in the creditor's possession is not an "act" to obtain possession or exercise control over property of the estate in contravention of 11 U.S.C. § 363(a)(3).<sup>633</sup> While nothing in 11 U.S.C. § 542(a) expressly requires a debtor to provide adequate protection as a precondition to turnover, neither does anything in 11 U.S.C. § 362 make it wrongful for a creditor to retain collateral legitimately in its possession merely because a bankruptcy petition has been filed.<sup>634</sup>

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<sup>626</sup> See Young, *supra* note 108, at 105; See 11 U.S.C. § 541 (a).

<sup>627</sup> See *Whiting Pools*, 462 U.S. 198.

<sup>628</sup> *Sharon*, 234 B.R. 676.

<sup>629</sup> Young, *supra* note 108, at 105.

<sup>630</sup> *Id.*

<sup>631</sup> *Id.*

<sup>632</sup> *Id.*

<sup>633</sup> See *U.S. Physicians*, 235 B.R. at 367.

<sup>634</sup> See *In re Nash*, 228 B.R. 669 (Bankr. N.D. Ill. 1999).

Hence, Judge Stosberg concluded, that a creditor is entitled to retain the vehicle or other collateral until the question of adequate protection is resolved.<sup>635</sup>

Two subsequent decisions, *In re Barringer*<sup>636</sup> and *In re Bernstein*<sup>637</sup> followed the reasoning of Judge Stosberg's dissent.<sup>638</sup> The majority opinion and Judge Stosberg's dissent in *Sharon*<sup>639</sup> provide cogent reasoning for the opposing points of view, both at the level of statutory interpretation and of policy analysis.<sup>640</sup> As the split of authority shows, the relevant statutes appear to be ambiguous in this context, and the controversy is likely to continue.<sup>641</sup>

#### Proposed legislative solutions:

Legislation considered in the 106<sup>th</sup> Congress in 1999 would have resolved the dispute in favor of the repossessing creditor.<sup>642</sup> Section 135 of H.R. 833 would have added a new Section 1307A to Chapter 13.<sup>643</sup> The proposed statute would have provided that, if a purchase money secured lender or a lessor of personal property had properly obtained possession of the property pre-petition, the creditor would be allowed to retain the property until it received adequate protection payments.<sup>644</sup> Such payments would have to be in the amount and frequency of the payments required in the underlying contract, unless the court, upon request, ordered lesser amounts or a different frequency.<sup>645</sup> The payments, however, could never be less frequent than monthly, and

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<sup>635</sup> See *Fitch*, 217 B.R. at 286.

<sup>636</sup> *In re Barringer*, 244 B.R. 402 (Bankr. E.D. Mich. 1999).

<sup>637</sup> *In re Bernstein*, 252 B.R. 143 (1995).

<sup>638</sup> Young, *supra* note 108, at 106.

<sup>639</sup> *Sharon*, 234 B.R. 676.

<sup>640</sup> Young, *supra* note 108, at 107.

<sup>641</sup> *Id.*

<sup>642</sup> *Id.*; See Hon. Eugene R. Wedoff, An Updated Analysis of the Consumer Bankruptcy Provisions of H.R. 833, Bankruptcy Reform Act of 1999, as Passed by the House, 30-32 (Nov. 1, 1999). [www.abiworld.org](http://www.abiworld.org)

<sup>643</sup> *Id.*

<sup>644</sup> *Id.*

<sup>645</sup> *Id.*

the amount could be no less than the depreciation of the collateral.<sup>646</sup> In addition, the debtor would be required to show that the property was insured no later than 60 days after the petition was filed.<sup>647</sup> Thus, the proposed legislation would have established the views expressed by Judge Stosberg's dissent in *Sharon*.<sup>648</sup>

Currently, a modified version of this proposal is included in H.R. 333 and in S. 420. The legislation now under consideration in the 107<sup>th</sup> Congress has eliminated the addition of a new Section 1307A to the Bankruptcy Code, and neither bill says anything explicitly about the rights of a secured creditor or a lessor of personal property that has lawfully taken possession of the property pre-petition.<sup>649</sup> Nonetheless, Section 309 of H.R. 333 and Section 309 of S. 420 would amend Section 1326(a) of Chapter 13 so as to require the debtor to make adequate protection payments within 30 days of the order for relief or within 30 days of the filing of a plan, whichever occurred sooner.<sup>650</sup> Moreover, within 60 days of the petition date, the debtor would have to show that the property was adequately insured.<sup>651</sup> These provisions would apply in all cases involving repossession.<sup>652</sup>

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<sup>646</sup> *Id.*

<sup>647</sup> *Id.*

<sup>648</sup> *Id.*; *Sharon*, 234 B.R. 676.

<sup>649</sup> *Id.*

<sup>650</sup> *Id.*

<sup>651</sup> *Id.*

<sup>652</sup> *Id.*

## VII. CONCLUSIONS:

As the dissent in the two panel opinions in *Gruntz I*<sup>653</sup> and *Gruntz II*<sup>654</sup> correctly observed, the chief concern of the majority appeared to be that allowing state courts to interpret the scope and applicability of the automatic stay would lead to unwarranted state court interference with bankruptcy administration, and to a plethora of state court judgments that would undermine orderly liquidation or reorganization. However, in the dissenting opinions in these two cases, Judge Fletcher displayed a deep concern with comity and federalism. State courts have jurisdiction to interpret and apply federal law unless Congress has deprived them of that right.<sup>655</sup> Federal courts should not purport to oust state courts of jurisdiction unless such a step is absolutely necessary to protect exclusive federal jurisdiction.<sup>656</sup> In fact, from a practical point of view, the decisions in *Gruntz*<sup>657</sup> could lead to strange consequences. For example, if an action were brought against the debtor in a state court, and if the state court determined that the stay did not apply, and went forward to render judgment in the debtor's favor, the judgment would have no binding effect because the state court would have had no jurisdiction to adjudicate the threshold jurisdictional issue of the stay's applicability.<sup>658</sup> The adverse party could bring another similar action in the bankruptcy court, or, if the action had been one over

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<sup>653</sup> *Gruntz I*, 166 F.3d 1020

<sup>654</sup> *Gruntz II*, 177 F.3d .

<sup>655</sup> *See Id.*

<sup>656</sup> *Id.*

<sup>657</sup> *In re Gruntz*, 166 F.3d 1020 (9<sup>th</sup> Cir.) (“*Gruntz I*”), opinion amended and superseded on reh’g, 177 F.3d 728 (9<sup>th</sup> Cir. ) (“*Gruntz II*”), reh’g en banc granted, opinion withdrawn, 177 F.3d 729 (9<sup>th</sup> Cir. 1999), opinion on reh’g, 202 F.3d 1074 (9<sup>th</sup> Cir. 2000) (“*Gruntz III*”).

<sup>658</sup> *See Young, supra* note 108, at 25.

which the bankruptcy court would have had no jurisdiction, the adverse party could seek relief from the stay and then go back to the original forum for a return match.<sup>659</sup>

The approach taken in *Singleton*,<sup>660</sup> *Siskin*,<sup>661</sup> and *Glass*<sup>662</sup> therefore, seems to be far more coherent than the views expressed in *Gruntz*.<sup>663</sup> Simply as a practical matter, holding that state courts have no jurisdiction to determine whether the stay applies could lead to all sorts of difficulties.<sup>664</sup> Thus, in my point of view, the best approach to deal with this issue of state court jurisdiction to determine applicability of the stay, would be for the aggrieved party to seek review before the state appellate courts, and ultimately, before the United States Supreme court. Federal courts should not be given the authority to determine whether state courts have jurisdiction when the automatic stay is at issue.

The issue of a non- bankruptcy tribunal's jurisdiction to impose sanctions for a violation of the stay has not arisen frequently. Moreover, the weight of authority holds that, even if a state court or other federal court has jurisdiction to determine whether the stay applies, only the bankruptcy court where the case is pending has jurisdiction to call a party to task for violating the stay.<sup>665</sup> On the one hand, exclusive bankruptcy jurisdiction over stay violation is essential to protect the bankruptcy court's exclusive jurisdiction over the bankruptcy estate and its property. On the other, it has long been settled that only the court whose authority has been violated has jurisdiction to impose sanctions on the offending party. Thus, state courts should not entertain

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<sup>659</sup> *Id.*

<sup>660</sup> *Singleton*, 230 B.R. at 535.

<sup>661</sup> *Siskin*, 258 B.R. 554.

<sup>662</sup> *Glass*, 240 B.R. 782.

<sup>663</sup> *In re Gruntz*, 166 F.3d 1020 (9<sup>th</sup> Cir.) (“Gruntz I”), opinion amended and superseded on reh’g, 177 F.3d 728 (9<sup>th</sup> Cir. ) (“Gruntz II”), reh’g en banc granted, opinion withdrawn, 177 F.3d 729 (9<sup>th</sup> Cir. 1999), opinion on reh’g, 202 F.3d 1074 (9<sup>th</sup> Cir. 2000) (“Gruntz III”).

<sup>664</sup> *See Young*, *supra* note 108 at 25.

<sup>665</sup> *See U.S. v. Barnett*, 330 F.2d 369 (5<sup>th</sup> Cir. 1963)(en banc), cert. 376 U.S. 681 (1964).

any claims involving sanctions for stay violations, and the same should remain within the exclusive realm of federal courts.

With respect to the issue as to whether repossession by creditor of debtor's property pre-petition, amounts to stay violation, legislation considered in the 106<sup>th</sup> Congress, which is discussed in detail above, would have resolved the dispute in favor of the repossessing creditor. Currently, a modified version of this proposal, included in H.R. 333 and in S. 420, which is also discussed in detail above, is now under consideration in 107<sup>th</sup> Congress. However, the legislation is silent whether the creditor could retain repossessed property until adequate protection payments were made. Presumably, however, Section 309 of H.R. 333 and of S. 420 would make it easier for creditors to argue that they should be allowed to retain repossessed property until the debtor has fulfilled the statutory duties, and that a failure by a debtor to do so should be grounds of relief from the stay. Judge Stosberg's dissent and the majority opinion in *Sharon*<sup>666</sup> provide cogent reasoning for the opposing points of view, both at the level of statutory interpretation, and of policy analysis. As the split of authority shows, the relevant statutes appear to be ambiguous in this context, and the controversy is likely to continue.

A provision in the above pending legislation making it mandatory on the part of the repossessing creditor to return the property, within a specific period of time, once adequate protection payments are made is likely to solve the above issue. This rule should be applicable even in cases of unsecured creditors, so as to ensure the benefit of all creditors.

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<sup>666</sup> Sharon, 234 B.R. 676 (6<sup>th</sup> Cir. B.A.P. 1999).

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32. *In re Mann*, 88 B.R. 427 (Bankr. S.D. Fla. 1998)
33. *N.L.R.B. v. Edward Cooper Painting, Inc.*, 804 F.2d 934 (6<sup>th</sup> Cir. 1986)
34. *In re Baldwin- United Corp. Litig.*, 765 F.2d 343 (2d Cir. 1985)
35. *In re Rimsat, Ltd.*, 98 F.3d 956 (7<sup>th</sup> Cir. 1996)
36. *In re Way*, 229 B.R. 11 (9<sup>th</sup> Cir. B.A.P. 1998)
37. *Labat v. Bank of Coweta*, 460 S.E. 2d 831 (Ga. Ct. App. 1995)
38. *Pemstein v. Stimpson*, 630 N.E.2d 608 (Mass. App. Ct. 1994)
39. *Martin-Trigona v. Champion Fed. Sav. & Loan Ass'n*, 892 F.2d 575 (7<sup>th</sup> Cir. 1989)
40. *Accord Pertuso v. Ford Motor Credit Co.*, 233 F.3d 417 (6<sup>th</sup> Cir. 2000)
41. *Ex parte Bradley*, 74 U.S. (7 Wall) 364 (1868)
42. *U.S. v. Barnett*, 330 F.2d 369 (5<sup>th</sup> Cir. 1963) (en banc), certified question answered, 376 U.S. 681 (1964)
43. *In re Schimmelpennicnk*, 183 F.3d 347 (5<sup>th</sup> Cir. 1999)
44. *In re Florio*, 229 B.R. 606 (S.D.N.Y. 1999)
45. *Hanna Coal Co. v. I.R.S.*, 218 B.R. 825 (W.D. Va. 1997)
46. *In re Pincombe*, 256 B.R. 774 (Bankr. N.D. Ill. 2000)

47. Shaddock v. Rodolakis, 221 B.R. 573 (D. Mass. 1998)
48. *In re* Diamond Indus. Corp., 265 B.R. 707 (Bankr. E.D. Va. 1999)
49. *In re* U.S. Physicians, Inc., 235 B.R. 267 (Bankr. E.D. Pa. 1999)
50. *In re* Lewis, 137 F.3d 1280 (11<sup>th</sup> Cir. 1998)
51. *In re* Knaus, 889 F.2d 773 (8<sup>th</sup> Cir. 1989)
52. *In re* Kalter, 257 B.R. 93 (M.D. Fla. 2000)
53. *In re* Regan, 264 B.R. 776 (Bankr. S.D. Fla. 2001)
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55. *In re* Baker, 264 B.R. 759 (Bankr. M.D. Fla. 2001)
56. United States v. Whiting Pools, Inc., 462 U.S. 198 (1983)
57. *In re* Belcher, 189 Bankr. 16 (Bankr. S.D. Fla., 1995)
58. *In re* Richardson, 135 B.R. 256 (Bankr. E.D. Tex. 1992)
59. *In re* Schwartz, 954 F.2d 569 (9<sup>th</sup> Cir. 1992)
60. *In re* Stringer, 847 F.2d 549 (9<sup>th</sup> Cir. 1988)
61. *In re* Johnson, 215 B.R. 381 (Bankr. N.D. Ill. 1997)
62. Charles R. Hall Motors, Inc. v. Lewis (*In re* Lewis), 137 F.3d 1280 (11<sup>th</sup> Cir. 1998)
63. *In re* Bernstein, 252 B.R. 143 (1995)
64. Koffman v. Ostioimplant Technology, Inc., 182 B.R. 115 (D. Md. 1995)