United States Bankruptcy Court
Western District of Wisconsin

Cite as: [Unpublished]

Paula L. McCoy, Plaintiff, v.
Billy R. McCoy and John E. Sanborn, Defendants
(In re Paula L. McCoy, Debtor)
Bankruptcy Case No. 95-32681-7; Adv. Case No. 95-3202-7

United States Bankruptcy Court
W.D. Wisconsin

May 6, 1996

Steven L. Vollmer, Grutzner S.C., Holland & Vollmer, Beloit, WI, for plaintiff.
Ralph E. Johnson, UAW-GM Legal Services, Janesville, WI, for defendant Billy McCoy.

Robert D. Martin, United States Bankruptcy Judge.

MEMORANDUM DECISION

Paula McCoy brought this adversary proceeding seeking sanctions and damages against her ex-spouse, Billy McCoy, and his divorce attorney, John Sanborn, for violating the discharge injunction of 11 U.S.C. § 524(a) and the Order of Discharge issued by this court on November 30, 1995. (Case no. 95-32681-7). The parties submitted the issue on briefs.

The McCoys were divorced in Rock County, Wisconsin, on September 28, 1994. The judgment of divorce included an award of custody and child support to Paula McCoy and a property settlement. Neither party was awarded maintenance or alimony. The property settlement included a hold harmless clause by which each McCoy agreed to take sole responsibility for certain jointly incurred debts.

On August 21, 1995, Paula McCoy filed a chapter 7 petition, listing Billy McCoy as an unsecured nonpriority creditor. On November 22, 1995, Billy McCoy filed an adversary proceeding seeking to make Paula McCoy's obligation under the hold harmless clause nondischargeable pursuant to 11 U.S.C. § 523(a)(15). An Order of Discharge was entered on November 30, 1995, and Billy McCoy received notice of that order.

This adversary proceeding stems from what quickly followed. On December 7, 1995, Billy McCoy, through his divorce attorney, John Sanborn, filed a motion in Rock County Circuit Court seeking an Order to Show Cause, captioned as an "Action to Modify or Enforce Judgment," against Paula McCoy. Specifically, the motion asked the court to modify his obligations under the property settlement,[(1)] to find Paula McCoy in contempt for failure to hold Billy McCoy harmless for an automobile loan, and to sanction her for failure to pay other debts related to the hold harmless clause. On December 12, 1995, Paula McCoy through her bankruptcy attorney, Steven Vollmer, sent a letter to Billy McCoy and John Sanborn stating that the Order to Show Cause

violated the discharge injunction. That same day, John Sanborn called Steven Vollmer and stated that Billy McCoy intended to pursue the state court action. The next day, December 13, 1995, Paula McCoy appeared without counsel in Rock County Circuit Court. The court continued the hearing until December 28, 1995, to permit Paula McCoy to obtain counsel. At the December 28 hearing, the Rock County court adjourned the matter until this court renders a decision in the pending § 523(a)(15) proceeding.

In seeking an injunction and sanctions against Billy McCoy and John Sanborn, Paula McCoy relies on 11 U.S.C. § 524(a) and the express language of the Order of Discharge. § 524 states in relevant part:

(a) A discharge in a case under this title--

(1) voids any judgment at any time obtained, to the extent that such judgment is a determination of the personal liability of the debtor with respect to any debt discharged under section 727, 944, 1141, 1228, or 1328 of this title, whether or not such discharge is waived;

(2) operates as an injunction against the commencement or continuation of an action, the employment of process, or an act, to collect, recover or offset any such debt as a personal liability of the debtor, whether or not discharge of such debt is waived[.]

The Order of Discharge states:

1. The above-named debtor is released from all dischargeable debts.

2. Any judgment heretofore or hereafter obtained in any court other than this court is null and void as a determination of the personal liability of the debtor with respect to any of the following;

(a) debts dischargeable under 11 U.S.C. § 523;

(b) unless heretofore or hereafter determined by order of this court to be nondischargeable, debts alleged to be excepted from discharge under clauses (2), (4), (6) and (15) of 11 U.S.C. Sec. 523(a);

(c) debts determined by this court to be discharged.

3. All creditors whose debts are discharged by this order and all creditors whose judgments are declared null and void by paragraph 2 above are enjoined from instituting or continuing any action or employing any process or engaging in any act to collect such debts as personal liabilities of the above-named debtor.

THIS ORDER DOES NOT AFFECT ANY PENDING ADVERSARY PROCEEDING TO DETERMINE DISCHARGEABILITY OF A PARTICULAR DEBT.

Billy McCoy and John Sanborn assert that "[t]he discharge injunction clearly was not . . . in effect for the debts relating to the divorce since those debts have not been discharged." The gist of this argument seems to be that divorce obligations subject to a timely challenge under any prong of § 523(a) are nondischargeable unless and until this court hold otherwise. The opposite is true. 11 U.S.C. § 524(a) applies to all debts involving personal liabilities, including those that may still be subject to action against a non-debtor co-signer or, in this case, former spouse. There is no disagreement in the courts about the scope of § 524(a). As one court recently noted, "[T]he few cases forced to actually decide the question state unequivocally that no actions *whatsoever* may be taken to assert a debtor's personal liability for a debt discharged in Chapter 7." In re

Martin, 157 B.R. 268, 275 (Bkrtcy. W.D. Va. 1993), citing Matter of Hunter, 970 F.2d 299 (7th Cir. 1992); Green v. Welsh, 956 F.2d 30 (2nd Cir. 1992); see also 3 *Collier on Bankruptcy* § 524.01[1] and [2] (Matthew Bender 1995).

Billy McCoy may and did file and prosecute a timely nondischargeability proceeding under § 523(a) without violating the discharge injunction. Furthermore, § 524(a) does not prevent Billy McCoy from pursuing a state court action to modify his obligations under the property settlement. But any argument that the Code allows Billy McCoy to attempt to enforce the hold harmless clause in derogation of the discharge injunction is without legal support.

Nonetheless, Mr. Sanford personally and on behalf of Mr. McCoy argues that their actions should be excused as having been taken in good faith. This contention is undercut by his complete ignorance of the plain language of the Order of Discharge issued by this court on November 30, 1995. That order expressly enjoins any action to collect "debts *alleged* to be excepted from discharge under clauses (2), (4), (6) and (15) of 11 U.S.C. Sec. 523(a)." (emphasis added). No reason has been advanced why the plain language of the discharge order can or should be ignored.

There is no other basis for finding that the defendants proceeded in good faith in the Rock County action. John Sanborn's scant brief contends, without saying more, that the state court action was filed out of concern "about waiver, estoppel or laches[,]" in an effort to "preserve" Billy McCoy's "interests" related to the hold harmless clause. This suggests that the defendants believed they had a legitimate state court cause to pursue. But the defendants misinterpreted Wisconsin law related to the modification of divorce judgments after one ex-spouse has discharged debts in bankruptcy.

Wisconsin state courts can and do modify the non-debtor's maintenance or support where the debtor ex-spouse's discharge of property settlement obligations in bankruptcy constitutes a "substantial change of circumstances" warranting an increase in the non-debtor's support. See In re Marriage of Eckert v. Eckert, 144 Wis.2d 770 (Wis. Ct. App. 1988); Spankowski v. Spankowski, 172 Wis.2d 285 (Wis. Ct. App. 1992), review denied, 497 N.W.2d 131 (Wis. 1993). These cases discuss at length the statutory, equitable, and policy reasons behind Wisconsin courts' willingness to revisit maintenance awards when a discharge negatively affects the non-debtor. That discussion leads to their specific refusal to review and modify a property settlement after a bankruptcy discharge. As explained in Spankowski, which appears to be the last time this issue was addressed by a Wisconsin appellate court:

We recognized [in Eckert] that the interest of a fresh start was considered less important by Congress than support obligations to a former spouse because those obligations are explicitly an exception to discharge through 11 U.S.C. § 523(a)(5). We also noted that a judge's determination of maintenance should be made according to the ability of the payor spouse to pay and after the consideration of everything affecting present and prospective matters relating to the lives of the divorcing parties. . . .

These justifications became the bases for our conclusion that the modification [of support] would not do "major damage" to the "clear and substantial" federal interests. Since Congress did not find the fresh start objective frustrated by allowing support debts to survive bankruptcy, it followed that a modification would not frustrate that objective either, especially since federal courts recognize that the subject of domestic relations is particularly suited to state control and the state law takes into consideration the financial position of the debtor.

Spankowski, 172 Wis.2d at 296-297 (citations omitted). The court refused to extend this rationale to property settlements, for two reasons. First, the court explained that

Congress had yet to pass a law specifically excepting property settlements from discharge. (The court noted, however, that a bill proposing to except property settlements was then pending in the House of Representatives). Id. at 297. Since property settlements were generally dischargeable, the court concluded, state court review of a property settlement runs a serious risk of offending the supremacy clause of the Constitution. Id. Moreover, since Wisconsin courts need not take into account the debtor ex-spouse's ability to pay before altering a property division, see Wis.Stat. § 806.07(1), any modification of the division "has a greater possibility of frustrating the debtor's fresh start." Id. at 298.

Two years after the Spankowski decision, Congress passed the bill referred to in that decision. Codified as 11 U.S.C. § 523(a)(15), the section excepts from discharge "any debt"

not of the kind described in paragraph (5) that is incurred by the debtor . . . in connection with a separation agreement, divorce decree or other order of a court of record, a determination made in accordance with State or territorial law by a government unit unless--

(A) the debtor does not have the ability to pay such debt from income or property of the debtor not reasonably necessary to be expended for the maintenance or support of the debtor or a dependent of the debtor, . . . or

(b) discharging such debt would result in a benefit to the debtor that outweighs the detrimental consequences to a spouse, former spouse, or child of the debtor[.]

Given the concerns expressed in Spankowski about offending the supremacy clause and frustrating the debtor's fresh start, it is virtually certain that Wisconsin courts will not review property settlement awards post-discharge after the passage of § 523(a)(15). Unlike § 523(a)(5), which grants the bankruptcy court jurisdiction to determine whether a debt is "actually in the nature of alimony, maintenance, or support" but no jurisdiction to determine whether the ordered support is equitable, § 523(a)(15) vests exclusive jurisdiction with the bankruptcy court to consider whether a property settlement obligation remains equitable and should be excepted from discharge. Therefore, at the time he filed his show cause motion in Rock County Circuit Court, Billy McCoy had no state-law "interest" in the hold harmless clause to preserve, as required by the doctrine of waiver, and no interest that could subsequently be lost through equitable estoppel or laches. See Bank of Sun Prairie v. Opstein, 86 Wis.2d 669, 273 N.W.2d 279 (1979) (discussing the doctrines of waiver, estoppel, and laches).

The defendants' good faith argument relies primarily on two cases, In re Worthing, 24 B.R. 774 (Bkrtcy. D.Conn. 1982), and In re Martin, 157 B.R. 268 (Bkrtcy. W.D. Va. 1993), where the court declined to impose a contempt order or hold the defendant liable for sanctions. In Worthing, the creditor's attempt to collect on the debt post-discharge did not violate the discharge injunction because the particular debt at issue was not listed on debtors' schedules and was not discharged pursuant to 11 U.S.C. § 523(a)(3). Because the debt was not discharged until the court concluded, after a hearing, that the creditor did in fact have constructive notice of the discharge (the creditor had received notice related to another debt that was listed), "there was not a specific and definite order enjoining collection of the subject debt." Worthing, 24 B.R. at 778. Worthing is distinguishable on its facts. Here, the defendants concede that the debt was listed and that they received actual notice of the discharge. Therefore, the Order of Discharge was "specific and definite" as to Paula's obligations to Billy. In re Martin is also distinguishable because the legal issues and, in particular, the procedural history and posture of that case were far more complicated than those at issue here. The Martin court "reluctantly" declined to impose sanctions on an attorney who violated the

discharge injunction only after concluding that, given the complexity of the legal and procedural issues involved, the attorney's mistake was relatively innocent. Martin, 157 B.R. at 277. In this case, the attorney's mistake appears to be based on ignorance and has many more of the indices of intentional harassment.

Contempt must be proved by clear and convincing evidence. Kimko Leasing, 144 B.R. at 1009. A number of cases suggest that the violation of the discharge order must be willful and knowing to justify contempt. See e.g. In re Martin, 157 B.R. at 277; Kimko Leasing, 144 B.R. at 1009-10. What these cases demonstrate, however, is that a creditor's post-discharge violation of the injunction is generally willful and knowing so long as the creditor has knowledge of the discharge and proceeds in the face of that knowledge. Ignorance of the effect of § 524 is no excuse.

The Seventh Circuit has not spoken on the issue, but the prevailing view is that a violation of the discharge injunction, like a violation of the automatic stay, is subject to the bankruptcy court's power to sanction contempt. See, e.g., In re Power Recovery Sys., Inc., 950 F.2d 798, 802 (1st Cir. 1991); In re Skinner, 917 F.2d 444, 449-50 (10th Cir. 1990); In re Walters, 868 F.2d 665, 670 (4th Cir. 1989); see also In re Mayex II Corp., 178 B.R. 464, 468 (Bkrtcy. W.D. Mo. 1995); In re Matthews, 184 B.R. 594, 598 (Bkrtcy. S.D. Ala. 1995); In re Stockbridge Funding Corp., 145 B.R. 797, 803-04 (Bkrtcy. S.D. N.Y. 1992); Kimko Leasing, Inc. v. Klee, 144 B.R. 1001, 1009 (N.D. Ind. 1992); In re Gallagher, 47 B.R. 92, 98 (Bkrtcy. W.D. Wis. 1985).

Bankruptcy courts can and do consider the legal sophistication of the client when determining whether sanctions are appropriate. Billy McCoy, operating on advice of counsel, may not be at fault. His culpability may be so slight as to require only a mild sanction for what is largely technical contempt. However, attorney John Sanborn's interpretation of § 524(a) is unreasonable and his clear misreading of the express language of the Order of Discharge is inexcusable. Unlike the situation described in Martin, this does not appear to be a case of an attorney proceeding on a "good faith, albeit mistaken, belief that [his] actions were permissible." Martin, 157 B.R. at 277. In Martin, the attorney did his homework, made an argument based on an extensive review of a schism between federal bankruptcy law and Virginia state law, and the court ultimately disagreed with the argument. Here, the evidence suggests that John Sanborn simply did not do his homework prior to filing the December 7, 1995, motion, and was not moved to do further research after being notified by Paula McCoy's counsel that he was proceeding in violation of the injunction.

Paula McCoy seeks an order declaring the defendants to be in civil contempt and reserving for further determination of the appropriate sanction. (Although the claim is for damages, "including time lost from work, costs, attorneys' fees, and any other damages proximately caused by the defendants' violation of the discharge order," the measure of the appropriate sanction may be considerably more limited by law and the facts of this case.) It may be so ordered.

END NOTE:

1. The divorce judgment called for Billy McCoy to pay $10,000 to Paula McCoy as part of an "equalizing payment," and an additional $4,000 plus interest accrued from the time of judgment, payable on or before September 28, 2004. Having paid the $10,000 prior to Paula McCoy's bankruptcy, he now seeks to have the $4,000 obligation expunged from the judgment.