No. 14-2151

UNITED STATES COURT OF APPEALS
FOR THE FIRST CIRCUIT

In re KEVIN CHARBONO,
Debtor

KEVIN CHARBONO,
Appellant

-v.-

LAWRENCE P. SUMSKI,
Chapter 13 trustee, Appellee

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEW HAMPSHIRE, NO. 13-471

BRIEF OF THE *AMICUS CURIAE* NATIONAL ASSOCIATION OF CONSUMER BANKRUPTCY ATTORNEYS IN SUPPORT OF THE DEBTOR APPELLANT AND SEEKING REVERSAL OF THE DISTRICT COURT'S DECISION.

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4) In all bankruptcy appeals, counsel for the debtor or trustee of the bankruptcy estate must list: 1) the debtor, if not identified in the case caption; 2) the members of the creditors' committee or the top 20 unsecured creditors; and, 3) any entity not named in the caption which is an active participant in the bankruptcy proceedings. If the debtor or trustee is not participating in the appeal, this information must be provided by appellant. NOT APPLICABLE.

/s/Tara Twomey
Attorney for the National Association of Consumer Bankruptcy Attorneys

Dated: February 25, 2015

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STATEMENT OF INTEREST OF *AMICUS CURIAE*

Incorporated in 1992, the National Association of Consumer Bankruptcy Attorneys ("NACBA") is a non-profit organization of more than 3,000 consumer bankruptcy attorneys nationwide.

NACBA's corporate purposes include education of the bankruptcy bar and the community at large on the uses and misuses of the consumer bankruptcy process. Additionally, NACBA advocates nationally on issues that cannot adequately be addressed by individual member attorneys. It is the only national association of attorneys organized for the specific purpose of protecting the rights of consumer bankruptcy debtors. NACBA has routinely filed *amicus curiae* briefs in various courts seeking to protect the rights of consumer bankruptcy debtors. *See e.g.*, *Schwab v. Reilly*, 560 U.S. 770 (2010); *Kawaauhau v. Geiger*, 523 U.S. 57 (1998); *In re Traverse*, 753 F.3d 19 (1st Cir. 2014); *In re Puffer*, 674 F.3d 78 (1st Cir. 2012). NACBA and its membership have a vital interest in the outcome of this case. NACBA members primarily represent individuals, many of whom file for protection under Chapter 13 and are required to provide copies of their tax returns during the pendency of the plan. Thus, any issue concerning the circumstances under which monetary sanctions may be imposed against them for the failure to comply with such plan requirements is of great significance to all such debtors.

STATEMENT UNDER FED. R. APP. P. 29(c)(5)

(a) No party's counsel authored this Amicus Curiae Brief in whole or in part;

(b) No party or party's counsel contributed money that was intended to fund preparing or submitting this brief; and

(c) No person, other than the amicus curiae, it members, or its counsel, contributed money that was intended to fund preparing or submitting the brief.

SUMMARY OF ARGUMENT

The proper test for determining the appropriateness of a sanction against a party in a bankruptcy court proceeding necessarily must take account for the unique circumstances of each case and the fundamental requirements of due process. Observation of these principles is particularly important when the situation involves a monetary sanction against the debtor in the form of a criminal contempt action, normally invoking the same due process concerns as a criminal prosecution. The "uniform" policy of the bankruptcy court in this case, which calls for the imposition of inescapable monetary sanctions as "punishment" against all debtors who fail to timely provide copies of their tax returns regardless of the reasons for the failure or whether it prejudiced the case in any way, directly contravenes these principles and threatens to directly undermine the integrity of the entire process and the fresh start bankruptcy is meant to provide.

Indeed, there is no basis for such a sanction against Charbono under the circumstances of this case; it is in fact tantamount to an unlawful "criminal contempt sanction." Yet, as it stands now, he is saddled with a monetary sanction he simply could not afford– and all because of an honest, inadvertent mistake that he rectified without any harm. The District Court's decision upholding this sanction must be reversed, along with the current "policy" of the bankruptcy court

that is permitting such inequitable results and frustrating the core rehabilitative purposes of Chapter 13 bankruptcy.

ARGUMENT

I

THE APPROPRIATENESS OF SANCTIONS MUST BE BASED UPON THE UNIQUE CIRCUMSTANCES OF EACHINDIVIDUAL CASE – NOT A UNIFORM POLICY OF AUTOMATIC SANCTIONS FOR A SPECIFIC TYPE OF CONDUCT – AND THE CIRCUMSTANCES IN THIS CASE DICTATE THAT NO SANCTION OF ANY VARIETY IS WARRANTED FOR CHARBONO'S HONEST, INADVERTENT, AND ULTIMATELY HARMLESS MISTAKE

A. The Sanctioning Powers of Bankruptcy Courts Have Clear Limitations, and Are to be Used Sparingly for Those Cases in Which a Party's Conduct Truly Warrants a Sanction Under the Specific Circumstances

Bankruptcy courts surely have the power to impose sanctions in the matters before them – consistent with the power '"inherent in all courts"' that is '"essential to the preservation of order,"' '"the enforcement of the judgments, orders, and writs,"' and '"the due administration of justice"' (*In re L.H. & A. Realty, Inc.*, 62 B.R. 910, 912-13 (Bankr. D. Vt. 1986) (quoting *Ex Parte Terry*, 128 U.S. 289, 295 (1888)), as well as the express grants of such power by statute and court rules (*see e.g.*, §§ 105(a), 1307(c), and Fed. R. Bankr. P. 9011, 9020). But there are clear limitations on the proper exercise of such power. '"The inherent power is not a broad reservoir of power, ready at an imperial hand, but a limited source; an

implied power squeezed from the need to make the court function."' *In re Paige*, 365 B.R. 632, 637-638 (Bankr. N.D. Tex. 2007) (quoting *Crowe v. Smith*, 151 F.3d 217, 226 (5th Cir.1998). "Courts' inherent sanctioning powers are likewise subordinate to valid statutory directives and prohibitions." *Law v. Siegel*, 134 S.Ct. 1188, 1194 (2014). "We have long held that whatever equitable powers remain in the bankruptcy courts must and can only be exercised within the confines of the Bankruptcy Code." *Id.* at 1194-95 (internal quotations omitted). The same is true of the expressly granted powers – they may only be exercised within the constraints of the Code. *Law,* 134 S. Ct. at 1194 (quoting 2 Collier on Bankruptcy ¶ 105.01[2], p. 105–6 (16th ed. 2013) ("It is hornbook law that § 105(a) 'does not allow the bankruptcy court to override explicit mandates of other sections of the Bankruptcy Code."').

There is a general "need for restraint and caution when assessing sanctions" given their potentially harsh consequences to the sanctioned party. *Paige*, 365 B.R. at 638. "The power to impose sanctions is a potent weapon and should, therefore, be deployed in a balanced manner. For that reason, proportionality is often a proxy for appropriateness." *Navarro-Ayala v. Nunez*, 968 F.2d 1421, 1426-27 (1st Cir. 1992). "[I]n fashioning a sanction, it is important that 'the punishment should be reasonably suited to the crime' . . . and the court must 'take pains [not] to use an elephant gun to slay a mouse."' *Navarro-Ayala,* 968 F.2d at 1427 (quoting

Anderson v. Beatrice Foods Co., 900 F.2d 388 (1st Cir. 1990)). Thus, the sanction power "should be used sparingly," bearing in mind "'[t]he fact that there is a law which compels certain conduct does not oblige a bankruptcy court to use its equitable powers to ensure compliance with that law.'" *Department of the Treasury for the Commonwealth of Puerto Rico v. Galarza-Pagan*, 279 B.R. 43, 46 (D.P.R. 2002). And any sanction, whatever the particular form, "must comport with procedural due process requirements." *In re Bushay*, 327 B.R. 695, 701 (B.A.P. 1st Cir. 2005); *Media Duplication Servs., Ltd. v. HDG Software, Inc.*, 928 F.2d 1228, 1238 (1st Cir. 1991). "[T]he determination of what process is due is, in part, a function of the type and severity of the sanction;" the greater the severity, the greater process normally due. *Media Duplication Servs., Ltd,* 928 F.2d at 1238.

Another crucial, firmly settled limitation upon the exercise of these general sanctioning powers is that the imposition of the sanction must be appropriate and reasonable under the totality of the circumstances, with particular focus upon whether the party's conduct was intentionally designed to, and in fact did, thwart proper administration of the case or unduly prejudice the rights of another party. "Several factors may be considered by the Court in determining whether to impose a sanction and what type of sanction to impose: whether the conduct was willful, or negligent; whether it was part of a pattern of activity, or an isolated event; whether it infected the entire pleading, or only one particular count or defense; whether the

person has engaged in similar conduct in other litigation; whether it was intended to injure; what effect it had on the litigation process in time or expense; whether the responsible person is trained in the law, what amount, given the financial resources of the responsible person, is needed to deter that person from repetition in the same case; and what amount is needed to deter similar activity by other litigants." *In re Eresian,* 487 B.R. 53, 68 (Bankr. D. Mass. 2013); *accord In re Thomson*, 329 B.R. 359, 362 (Bankr. W.D. Mass. 2005); *In re CK Liquidation Corp.*, 321 B.R. 355, 362 (B.A.P. 1st Cir. 2005). "This is not an exhaustive list of the factors that may be considered," *Thomson,* 329 B.R. at 362, because a court's determination of what may constitute an appropriate sanction "requires a case-by-case evaluation of all of the attendant circumstances" *In re Eddy*, 339 B.R. 8, 15 (Bankr. D. Mass. 2006); *In re Taal*, 520 B.R. 370, 375 (Bankr. D.N.H. 2014).

Some courts even require a specific finding of "bad faith" to warrant any exercise of the sanctioning power, such that the '"very temple of justice has been defiled"' by the sanctioned party's conduct. *Paige*, 365 B.R. at 637-38 (quoting *Goldin v. Bartholow*, 166 F.3d 710, 722 (5th Cir. 1999)). That is the case in this circuit for dismissal or conversion sanctions under section 1307(c). The party seeking imposition of such sanctions bears the burden of proving the debtor acted in "bad faith" – which "requires some form of deception," *In re Taal*, 520 B.R. at 375) (internal quotations omitted), and which is based upon similar factors

designed to assess the existence and degree of any misconduct on the part of the debtor: that is, "the debtor's honesty in the bankruptcy process," including whether he has "attempted to mislead the court" or "made any misrepresentations," and the debtor's "motivation and sincerity in seeking Chapter 13 relief. *Id.* at 375.

At the least, however, it is uniformly clear that the sanctioning power is not appropriately invoked in response to mere inadvertent mistakes or carelessness. The power should instead be reserved for "egregious" conduct, *In re Coquico, Inc.*, 508 B.R. 929, 941 (Bankr. E.D. Pa. 2014), "willful misconduct," *In re Brown*, 408 B.R. 509, 525 (Bankr. D. Idaho 2009; *In re Eddy*, 339 B.R. at 16-17), "a reckless disregard for the truth and for the rights of . . . creditors," *In re Pettey*, 288 B.R. 14, 21 (Bankr. D. Mass. 2003), conduct intended to "continually vex and harass adverse parties and the Court," *In re Eresian*, 487 B.R. at 68-69; *In re Kristan*, 395 B.R. 500, 509-510 (B.A.P. 1st Cir. 2008), or some other "egregious abuse of the Bankruptcy Code," *Pettey,* 288 B.R. at 16. When it is the debtor at issue, "[t]he bottom line is whether the debtor is attempting to thwart his creditors, or is making an honest effort to repay them to the best of his ability." *In re Sullivan*, 326 B.R. 204, 212 (B.A.P. 1st Cir. 2005). The general focus upon the debtor's "good faith" in connection with the process "advance[s] one of the primary purposes of bankruptcy, which is to relieve the honest but unfortunate debtor from the weight of oppressive indebtedness, allowing the debtor to start afresh." *Id.* at 211-12.

Thus, for example, even if the debtor has technically "defaulted" under a significant or "material" term of a Chapter 13 plan, courts will not apply the sanction of dismissal or conversion under section 1307(c) when it would frustrate this primary purpose of the Code. "[T]he mutuality of interests in most chapter 13 cases between the claimants and the debtors would prompt a common effort to facilitate the curing of defaults rather than the insistence upon conversion or dismissal." *In re Faaland*, 37 B.R. 407, 409 (Bankr. D.N.D. 1984); *accord In re Jarvis*, 24 B.R. 46, 48 (Bankr. D. Vt. 1982). "Dismissing or converting a case for a material default under § 1307(c)(6) is a discretionary matter and is appropriate when a debtor is unable to cure a default and the plan cannot be modified to make completion feasible." *In re Hutchens*, 480 B.R. 374, 387 (Bankr. M.D. Fla. 2012); *accord In re Grant*, 428 B.R. 504, 506-07 (Bankr. N.D. Ill. 2010). So unintentional defaults do not warrant such sanction if the plan can still be achieved. *See Jarvis,* 24 B.R. at 47 ("If the Court were to construe a failure of the Debtors to make the payments to the bank under the particular circumstances of this case a material default, it would, in effect, override the rehabilitative purpose of Chapter 13."); *Faaland,* 37 B.R. at 16 (although "the Debtors were in violation of the plan through their default," "the default was caused by their diminished employment due to bad weather" – and thus "it would be inequitable to dismiss the Chapter 13 Plan").

Moreover, because the appropriateness of sanctions is ultimately based upon a "general balancing of equities," *Taal*, 520 B.R. at 375, even if a monetary sanction may be justified, courts will not impose it when doing so would be unduly harsh or unnecessarily impede proper administration of the case. As a general matter, "a higher standard of due process protection" is required for the imposition of a monetary sanction, *Media Duplication Servs., Ltd.*, 928 F.2d at 1238, and such a sanction must be "narrowly drawn to accomplish the dual objectives of compensating aggrieved parties and coercing compliance with the court's orders" *In re Clark*, 91 B.R. 324, 339 (Bankr. E.D. Pa. 1988). "[A]dditional considerations come into play when such monetary sanctions are imposed by a bankruptcy court against a debtor in bankruptcy." *Id.* at 338. "[M]onetary claims against debtors should normally be relegated to the bankruptcy claims process, along with the other claims taxing the debtor's available resources, in furtherance of the basic tenets that creditors should share equally in the distribution of the debtor's estate. *Id.* In light of these considerations, monetary sanctions against the debtor may be inherently unenforceable or inequitable, potentially requiring even further restraint in any exercise of the sanctioning power. *See, e.g.*, *In re Jones*, 174 B.R. 8, 14 (Bankr. D.N.H. 1994) (where the court denied the trustee's request for monetary sanctions because the debtor lacked stable income or other assets and thus such sanctions would simply "further impose hardship upon the debtor's family, which

is not the purpose of imposing sanctions"); *Pettey*, 288 B.R. at 21 (declining to impose a monetary sanction, the court reasoned: "a monetary sanction (such as an award of fees) might have no deterrent effect, as further monetary obligations would only compete with existing obligations that are long overdue").

B. The Power to Impose Inescapable Monetary Sanctions as "Punishment" for a Party's Past Transgressions is Even Further Circumscribed

In addition to the foregoing principles placing general limitations on the forms of permissible sanctions in a bankruptcy court, the exercise of sanctioning power is further circumscribed, if not completely precluded, when the penalty imposed effectively takes the form of a "*criminal* contempt sanction." It is widely understood that a bankruptcy court's power to control contemptuous conduct is, by its very nature, in the form of a *civil* contempt sanction. "The full contempt power of the bankruptcy court is limited to core proceedings by the derivative jurisdictional grant in 28 U.S.C. section 157 and to civil contempt by the terms of 11 U.S.C. section 105(a)." *In re L.H. & A. Realty*, 62 B.R. at 913-14; *see also In re Fatsis*, 405 B.R. 1, 7 (B.A.P.1st Cir. 2009) (quoting *Goya Foods, Inc. v. Wallack Mgmt. Co.*, 290 F.3d 63, 78 (1st Cir. 2002) ("Federal courts are empowered to issue civil contempt sanctions to 'protect[ ] the due and orderly administration of justice and ... maintain [ ] the authority and dignity of the court.'"); *In re Eddy*, 339 B.R. at 17 ("a bankruptcy court has the authority to impose civil contempt sanctions for failure to comply with a prior court order").

"Congress has safeguarded the constitutionality of the bankruptcy court's circumscribed contempt power by making the power contingent on the reference of bankruptcy cases and proceedings from the district court [citation], confining it to orders issued within core proceedings . . ." *In re L.H. & A. Realty, Inc.*, 62 B.R. at 912. "[28 U.S.C.] Section 1481 grants the Bankruptcy Court 'the powers of a court of equity, law, and admiralty' but limits the court's power to punish a *criminal* contemnor to situations where the contemptuous conduct occurred in the judge's presence." *In re Better Homes of Virginia, Inc.*, 52 B.R. 426, 429 (E.D. Va. 1985) (italics original). While "civil or coercive contempt actions are 'necessary' and appropriate' to effectuate [the court's orders] . . . criminal contempt actions are necessary only to vindicate the dignity of the court and are *collateral* to the bankruptcy proceeding." *Id.* at 430 (italics original); *see also In re L.H. & A. Realty, Inc.*, 62 B.R. at 912 (a "criminal contempt" action "involves an independent, collateral proceeding"). Accordingly, '"bankruptcy courts have no statutory basis for criminal contempt power as to contempt not committed in their presence."' *In re Lawrence*, 164 B.R. 73, 75 (W.D. Mich. 1993) (quoting *Matter of Hipp*, 895 F.2d 1503, 1515 (1990)); *see also In re Jolly Joint, Inc.*, 23 B.R. 395, 402 (Bankr. E.D. N.Y. 1982) ("Pursuant to 28 U.S.C. § 1481, the court is precluded from punishing a criminal contempt not committed in its presence.")

Thus, courts have declined to impose penalties on the order of criminal contempt sanctions directly within the context of the core bankruptcy proceedings. *See e.g., Jolly Joint*, 23 B.R. at 402 (although the debtors had engaged in contemptuous conduct clearly warranting sanctions, the proceedings on the matter had been "of the civil variety," which were insufficient to support a finding of criminal contempt, and thus the court directed initiation of criminal contempt proceedings "[i]n order to give the defendants the full measure of procedural safeguards that are due them"); *In re Brown*, 408 B.R. 509, 525-26 (Bankr. D. Idaho 2009) (declining to impose a monetary sanction otherwise warranted for a party's "willful" misconduct and "bad faith" because the party to be sanctioned "would not be able to reduce or avoid the fine through compliance" and thus imposing the sanction would be tantamount to a criminal contempt sanction).

To whatever extent a bankruptcy court may properly a conduct criminal contempt action as part of the "core" bankruptcy proceeding or within a "collateral" proceeding, "[t]he contemnor in a criminal contempt case is entitled to a hearing, proof beyond a reasonable doubt and all the protections afforded those accused of a crime." *In re Power Recovery Sys., Inc.*, 950 F.2d 798, 802, n.18 (1st Cir. 1991) (citing Fed. R. Crim. P. 42(b)); *see also In re Armstrong*, 302 B.R. 432, 437 (B.A.P. 10th Cir. 2004) ("criminal contempt sanctions may not be imposed upon a contemnor unless he has been afforded the necessary Constitutional

protections"); *Jolly Joint*, 23 B.R. at 403 ("In a criminal contempt proceeding, the defendants must be accorded the fundamental protections of criminal procedure."). Therefore, it is crucial to distinguish between the two types of contempt sanctions in determining if a particular sanction is appropriate and comports with the requirements of due process. *Better Homes*, 52 B.R. at 430.

"In deciding whether a proceeding before a lower court involves civil or criminal contempt, we are required to look to the purpose and character of the sanctions imposed, rather than to the label given to the proceeding by the court below." *Power Recovery Systems*, 950 F.2d at 802. '"Civil contempt sanctions are designed to coerce the contemnor into compliance with a court order or to compensate a harmed party for losses sustained."' *In re Duby*, 451 B.R. 664, 670 (B.A.P. 1st Cir. 2011) (quoting *United States v. United Mine Workers of Am.*, 330 U.S. 258, 303–304 (1947)). "In contrast, criminal contempt sanctions are punitive in nature and are imposed for the purpose of vindicating the authority of the court." *Duby,* 451 B.R. at 670. "Accordingly, compliance with the court's command will not lift the sanction." *Jolly Joint,* 23 B.R. at 403. Ultimately then, if '"the contemnor is able to purge the contempt and obtain his release by committing an affirmative act,"' the sanction is civil in nature, whereas '"a completed act of disobedience that the contemnor cannot avoid is criminal in nature.'" *In re Van Vleet*, 461 B.R. 62, 69 (D. Colo. 2010) (quoting *In re Lucre Management Group,*

L.L.C., 365 F.3d 874, 877 (10th Cir. 2004)); *accord Clark*, 96 B.R. at 337. As such, "'a flat, unconditional fine' totaling even as little as $50 announced after a finding of contempt is criminal if the contemnor has no subsequent opportunity to reduce or avoid the fine through compliance."' *Armstrong* 302 B.R. at 437 (quoting *International Union, United Mine Workers of Am. v. Bagwell*, 512 U.S. 821, 829 (1994); *accord In re Dyer*, 322 F.3d 1178, 1192 (9th Cir. 2003).

C. Under the Circumstances of This Case, There is No Basis for a Sanction Against Charbono – "Criminal," "Civil," or of Any Other Variety

Here, it is undisputed that Charbono – an "extremely unsophisticated," "incredibly low functioning" debtor who supports his disabled wife and family with meager income from yard maintenance work and food stamps (Appendix to Opening Brief [App.] 13-15, 28, 36) – made an honest mistake in failing to timely provide the trustee a copy of the request for an extension of time to file the family's 2013 tax return, as required under the plan terms (App. 18 [Charbono was required to provide a copy of this document within seven days of its filing]). Charbono had filed for the extension because he could not afford to pay for the preparation of the tax return before the deadline of April 15th, and he believed his wife – who was undergoing "electro-convulsion shock therapy" at the time and yet was still "the high-functioning member of the household" – had provided the trustee with the required copy of the extension. (App. 28, 50-51, 58.) It is also undisputed that: (1) after being put on notice of this inadvertent mistake,

Charbono's wife provided a copy of the extension to the trustee before the September 20, 2013, hearing on the motion to dismiss Charbono's case or impose sanctions against him for the untimely compliance; (2) the extension was granted, such that the tax return was not due until October 15, 2013; and (3) there was no conceivable possibility that Charbono would receive any sort of tax refund – much less a refund in excess of $1,200 for the benefit of the creditors (App. 38-39, 42, 57-58 [the trustee "stipulated" to this fact]; Appellee's Brief (U.S.D.C.) 7 [same]).[1]

Moreover, there has never been any doubt that a monetary sanction under these circumstances could be characterized as anything but an unavoidable penalty for Charbono's past failure to timely comply with this term of the plan. (Addendum to Opening Brief [Add.] 9 [where the District Court noted this was "meant as punishment for Charbono's past failure to timely comply"]; Appellee's Brief 8 [where the trustee says this was "admittedly" to "punish" Charbono].) Regardless of how else one may try to "label" it (see Appellees' Brief 5 [where the trustee notes that neither he nor the bankruptcy court characterized the penalty as a "contempt sanction"]), "we are required to look to the purpose and character of the sanctions imposed" *Power Recovery Sys., Inc.*, 950 F.2d at 802. Because Charbono had "no subsequent opportunity to reduce or avoid the fine through compliance," it indisputably was a "criminal contempt sanction," *Bagwell*, 512 U.S. at 829,

[1] Charbono was required to remit "all tax refunds *in excess of $1,200* . . . as additional disposable income to fund the plan." (App. 16, emphasis added.)

entitling him to "all the protections afforded those accused of a crime." *Power Recovery Sys., Inc.* 950 F.2d at 802, n.18. Yet, Charbono was not accorded these protections. This alone invalidates the sanction. *Power Recovery Systems,* 950 F.2d at 802; *Bagwell,* 512 U.S. at 829; *L.H. & A. Realty*, 62 B.R. at 913-14; *Armstrong*, 302 B.R. at 437; *see also* Fed. R. Crim. P. 42(b).

Even entertaining the notion that this fundamental failure of due process could be ignored by somehow characterizing the sanction as merely "civil" in nature, it still could not stand under any of the permissible bases for civil sanctions. Both the District Court and the trustee ultimately couch this sanction as a permissible under the bankruptcy court's "inherent" sanctioning power and its statutorily granted sanctioning powers under sections 1307(c)(6) and 105(a). (Add. 6, 11, 13-14; Appellee's Brief 5, 6-8.) The fundamental problem with their rationale is that it seeks to apply the fixed penalty against Charbono *regardless* of whether the particular circumstances of his case would warrant a sanction. The District Court even characterized Charbono's inadvertent mistake here as merely a "modest transgression," which was "far less culpable in nature" than the sort of "intentional or reckless" conduct warranting a criminal sanction. (App. 13.) Indeed, it was "far less culpable in nature" than what would warrant a *civil* sanction based on the analysis above demonstrating that sanctions of any form – particularly monetary sanctions against an already struggling debtor – are generally

reserved for clearly "egregious" or "abusive" conduct specifically designed to thwart the proper administration of the case or the rights of creditors. *See, e.g., Pettey*, 288 B.R. at 21; *Jones*, 174 B.R. at 14; *Taal*, 520 B.R. at 375.

The only purported justification for ignoring the undisputed fundamental fact of Charbono's *un*intentional, *non*-reckless failure to timely provide a copy of the extension request is the pursuit of a "uniform" or "standard" policy penalizing debtors for any and all such transgressions for the purpose of bringing "attention" to the general need to comply with such plan terms. (App. 34-35-36, 49, 61-62.) But a "uniform" treatment of all cases is exactly what the case law prohibits: it is clear that the appropriateness of a sanction must be based upon the "totality of the circumstances," *Taal*, 520 B.R. at 375, with the primary focus being whether "the debtor is attempting to thwart his creditors, or is making an honest effort to repay them to the best of his ability." *Sullivan*, 326 B.R. at 212. There is no indication in the record – nor has anyone even ventured to claim – that Charbono is or has been anything but an honest debtor making his best effort to repay his creditors in accordance with the fundamental terms of the plan.

In fact, the factors relevant to determining the appropriateness of a sanction weigh decidedly against any sort of penalty for Charbono's inadvertent, "modest transgression" of a technical requirement: it was at most "negligent," not "willful;" it was "an isolated event," not "part of a pattern" of similar activity; it did not

"infect" the entire process, but was instead clearly harmless, as Charbono's wife provided a copy of the extension after Charbono was put on notice of the problem; it was not "intended to injure," as Charbono in fact believed, albeit erroneously, that his wife provided the copy within the required time period; and, given his undisputed "extreme[] unsophisticat[ion]," there is no basis for holding him to the standard of a person who is "trained in the law." *Thomson*, 329 B.R. at 362.

The single remaining factor that the penalty may have value as a "deterrent" against future transgressions of this kind, *see id.*, cannot tip the scales in the other direction, particularly when one considers the countervailing concerns of unnecessarily burdening honest debtors like Charbono with additional obligations that would frustrate the Code's purpose of providing them a meaningful opportunity for a fresh start. *Sullivan*, 326 B.R. at 211. For someone like Charbono, whom the District Court itself described as being "in dire straits" (App. 60), imposing a monetary sanction against him would force him into the untenable position of forgoing some other essential financial need of his family to make up for the shortfall that month: "does the debtor not pay the Trustee; does the debtor not pay the mortgage; does the debtor not buy groceries?" (App. 49.) It makes no sense to potentially derail an otherwise viable repayment plan in pursuit of a penalty for an inadvertent mistake that was cured with no prejudice to anyone, which is precisely why the appropriateness of a sanction is and must remain a

determination that is based upon the totality of the circumstances in a given case. A court's ability to consider the unique situation that brought about the conduct at issue is crucial to a proper "balancing of equities." *Taal*, 520 B.R. at 375.

Indeed, in articulating the purported need to follow the "uniform" policy of imposing such sanctions regardless of the individual circumstances, the bankruptcy court repeatedly characterized the situation as an all-or-nothing scenario in which it was compelled to impose the sanction to avert dismissal. (App. 40, 45-46, 47, 52, 54, 61.) Most poignantly here, the court stated: "All right. Fine. Then if I adopt [Charbono's] argument [that a monetary sanction is impermissible] I'm going to dismiss this case today on [the trustee's] motion . . ." because "[t]here's no other option." (App. 54.) The court's rationale was evidently based on the notion that the failure to timely comply with the document turn-over provision constituted a "material default" under section 1307(c)(6) and thus compelled dismissal absent some other action to penalize Charbono for the transgression. The trustee puts forth the same sort of rationale in defense of the monetary sanction in essentially arguing that, because the court had the power to dismiss the case on account of this default, it surely had the power to impose a monetary sanction. (Appellee's Brief 5.)

But even the District Court recognized that, as section 1307(c)(6) expressly states (italics added) – "the court *may* convert as case . . . or *may* dismiss a case . . . for cause, including [¶ . . . ¶] material default by the debtor with respect to a term

of a confirmed plan" – a bankruptcy court is "empowered to dismiss, or convert, but it is not compelled to do either" and "it may do nothing . . ." (App. 14.) So the bankruptcy court was not left in some sort of paradoxical situation that *compelled* it to impose a *monetary* sanction to rescue the case from certain demise and thus justified dispensing with the requirements of fundamental due process. Section 1307(c) does not even provide a basis for imposing a monetary sanction, as it solely empowers the court to "dismiss" or "convert" a case upon proof of a "material default" under a plan. *See In re Zizza*, 500 B.R. 288, 292 (B.A.P. 1st Cir. 2013) (construing section 1307(c) in this limited manner); *Grant*, 428 B.R. at 506 (same); *In re Elmore*, 94 B.R. 670, 678 (Bankr. C.D. Cal. 1988) (same).

Moreover, this was not a "material default" warranting any sort of sanction under section 1307(c)(6). Again, the "totality of the circumstances" test applies in this context as well, *Taal*, 520 B.R. at 375; *Sullivan*, 326 B.R. at 211, and no type of sanction could be deemed appropriate under these circumstances because, even though Charbono failed to timely comply with a term of the plan, there was no "deception," "unfair[] manipulat[ion]," or other prejudicial abuse of the process – this was instead an inadvertent harmless mistake that Charbono rectified after being put on notice of the problem. *Taal,* 520 B.R. at 375-76. As noted, a debtor's curing of a default on a particular term of the plan under such circumstances normally precludes a finding of "material default," so as to permit the plan to

proceed and achieve its ultimate goals of rehabilitation and repayment. *Faaland*, 37 B.R. at 409; *Jarvis*, 24 B.R. at 48; *Hutchens*, 480 B.R. at 387; *Grant*, 428 B.R. at 506-07; *see also* 8 Collier on Bankruptcy ¶ 1307.04[6] (Alan N. Resnick & Henry J. Sommer eds., 16th ed.) ("When the default is caused by unexpected circumstances beyond the debtor's control that have been remedied, the court may find that it is not a material default.").

As a recent case in point, the trustee in *Galarza-Pagan*, 279 B.R. at 43, sought the dismissal sanction against the debtors under section 1307(c) on the basis that they had failed to timely provide their tax returns in accordance with the plan. *Id.* at 45, 48. But the bankruptcy court refused to dismiss the case, finding the debtors "did not commit any egregious behavior which would warrant a finding of bad faith." *Id.* at 48. The district court affirmed, agreeing with the bankruptcy court and further noting that "the binding nature of confirmed plans" was a policy consideration in favor of finding a dismissal sanction inappropriate under the circumstances. *Id.* This is consistent with the general policy of declining to impose sanctions for the violation of a particular term of the plan when doing so would pose a hardship upon an already struggling debtor and thereby place the entire plan in jeopardy of failing. *See Jones*, 174 B.R. at 14; *Pettey*, 288 B.R. at 21.[2]

[2] This situation is quite different than those in which courts have found a dismissal sanction was properly imposed for a debtor's failure to file the required prepetition tax returns under section 1307(e). *See Howard v. Lexington Inv., Inc.*, 284 F.3d

The equitable and policy considerations that ultimately drive the sanctions analysis simply compel the conclusion that, even if Charbono's failure to timely comply with this term of the plan could properly be construed as a "material default" under section 1307(c) or some form of misconduct otherwise warranting monetary sanctions under the bankruptcy court's other sanctioning powers, such a sanction cannot satisfy the test of "appropriateness" under the totality of the circumstances.

D. The "Uniform" Policy of Automatic Sanctions Has Far-Reaching Implications Threatening to Derail the Plans of Untold Honest Debtors

The problems Charbono would face, saddled with the burden of a monetary sanction he simply cannot afford to pay along with his other expenses foreshadow the problem other similarly situated debtors would face in the event they make this mistake and become the target of the "uniform" sanction policy. In fact, the trustee emphatically states that he intends to continue this practice of pursuing monetary sanctions in all such situations regardless of the circumstances. (Appellee's Brief

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320 (1st Cir. 2002); *In re Maclean*, 200 B.R. 417 (Bankr. M.D. Fla. 1996). First, unlike the permissive form of the remedy under section 1307(c), the remedy under section 1307(e) is stated in mandatory terms – namely, if the debtor fails to file all tax returns for the four-year prepetition period within the time specified under section 1308(a), upon a noticed motion, "the court *shall* dismiss . . . or convert . . . the case. § 1307(e). Second, and more importantly, in those cases dismissal was warranted because the debtor displayed clear disregard for the requirement by ignoring further orders to comply and the failure to timely provide the returns prejudiced the proper administration of the case, since the returns were essential to establishing a confirmable plan. *Howard,* 284 F.3d at 323; *Maclean* 200 B.R. at 418.

9.) Further, he not only acknowledges that the amount of the sanction currently sought under his practice is "entirely arbitrary" but also indicates that he can and will seek higher sanctions as he deems appropriate –"[u]nless, due to an order in Charbono's favor regarding this appeal, the Bankruptcy Court is found *not* to have the power to impose" such sanctions. *Id.* (italics original). Indeed, without a ruling in Charbono's favor on appeal, the trustee may well be successful in obtaining even greater monetary sanctions against debtors, particularly so long as the bankruptcy court continues to believe it can and should operate in tandem with this "uniform" sanctioning policy.

Thus, as the situation currently stands, honest debtors like Charbono who seek bankruptcy relief specifically because of financial "dire straits" would be forced to carve out a portion of their fixed budgets, which already devote all disposable income to payment of creditors, to pay the monetary sanction. The resulting void in the monthly resources would place them in jeopardy of losing the essential protections of bankruptcy they need, as they must choose between paying the trustee or covering essentials like food and gas for traveling to work. Those who cannot scrounge up the additional money face the prospect of defaulting on the most material term of all – the plan payment term, and *that* is what would lead to "the death penalty" of dismissal in the case, *not* the absence of a monetary sanction as the trustee postulates. Appellee's Brief 11; *see In re Witkowski*, 523

B.R. 300, 306-07 (B.A.P. 1st Cir. 2014) (internal quotations omitted) (the debtor's failure to make the plan payments "easily justifie[d] the dismissal of her Chapter 13 case," as "[b]ankruptcy courts within this circuit have long held that a debtor's failure to make payments to the chapter 13 trustee as required by § 1326, by itself, is grounds for dismissal . . . [listing numerous cases to illustrate this point]").

Perhaps in some cases a monetary sanction would be warranted for the failure to comply with this sort of document turn-over provision, such as where the failure to comply was coupled with facts showing an obvious intent to thwart, or a reckless disregard for, the proper administration of the case, along with some kind of prejudice resulting from the failure to timely comply – although the sanction would still have to satisfy the fundamental requirements of due process if it was imposed as "punishment" for a past transgression from which there is no escape. But that is not what we have in cases like this one, where the failure to comply is the inadvertent mistake of an honest, unsophisticated debtor who cures the situation after being notified of the problem and whose financial situation is so delicately balanced that forcing him to pay this penalty could shut him out of the process. The ultimate impact of this "uniform" policy of automatic sanctions is to deprive debtors like Charbono of the bankruptcy relief for which they are particularly suited, while also potentially depriving the creditors of any recovery

on their claims. The resulting waste of resources and unnecessary frustration of the Code's core rehabilitative purposes simply cannot and should not be countenanced.

Under the proper analysis, which takes into account the particular circumstances of the debtor's situation, no form of monetary sanction against Charbono can be deemed appropriate. Having relied upon an erroneous understanding and application of its sanctioning powers to impose the monetary sanction in this case, the bankruptcy court's imposition of the sanction must be reversed as an abuse of discretion. *United States v. One Star Class Sloop Sailboat*, 546 F.3d 26, 37 (1st. Cir. 2008) ("an error of law is always tantamount to an abuse of discretion").

CONCLUSION

For these reasons, NACBA respectfully requests that this Court reverse the District Court's order affirming the bankruptcy court's sanction against Charbono.

CERTIFICATION OF COMPLIANCE
WITH TYPE-VOLUME LIMITATION

I hereby certify that the foregoing Brief contains fewer than 6,425 words, excluding the parts of the Brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii). In preparing this certification, I relied on the word-processing system used to prepare the foregoing Brief.

The foregoing Brief complies with the typeface requirements of Fed. R. App. P. 32(a)(5) and the type style requirements of Fed. R. App. P. 32(a)(6) because it was prepared in a proportionally spaced typeface using Microsoft Word in 14-point Times New Roman font, except for footnotes and electronic signatures.

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CERTIFICATE OF SERVICE

I hereby certify that I served the within Brief of Amicus Curiae, The National Association of Consumer Bankruptcy Attorneys, on counsel for all parties, electronically through the ECF System, on this 25th day of February, 2015.

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