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**EDITOR'S NOTE: BANKRUPTCY AND BANKS**

Steven A. Meyerowitz

**BANKRUPTCY ALTERNATIVES TO TITLE II OF THE DODD-FRANK ACT—  
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**VIOLATING A DEBTOR'S DISCHARGE INJUNCTION: LENDERS BEWARE**

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**BANKING BRIEFS**

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# Violating a Debtor's Discharge Injunction: Lenders Beware

*Michael J. Lichtenstein\**

*Failing to adhere to, or simply ignoring, a notice of a debtor's discharge injunction can often lead to the imposition of sanctions, including punitive damages. These kinds of violations, even though not malicious in nature, are frequently deemed to be willful and can be easily avoided. The author of this article discusses bankruptcy discharges and the perils of violating discharge injunctions.*

The primary goal of every individual debtor who files for bankruptcy is to obtain a discharge. Once obtained, the debtor is relieved from any debts encompassed in the discharge. Accompanying a bankruptcy discharge is an injunction which prevents creditors from pursuing claims that have been discharged. Unfortunately, sometimes lenders with automated billing systems neglect to adjust the program to terminate invoicing and collection attempts from discharged debts. This can be a costly lesson as courts have held that such violations can subject creditors and their counsel to contempt citations and monetary sanctions.

## **A DISCHARGE IN BANKRUPTCY**

An individual debtor's overall goal is to obtain a discharge will that relieve him from having to pay his outstanding debts in full, either through a Chapter 11 or Chapter 13 reorganization plan or through a Chapter 7 liquidation. In a Chapter 7 proceeding, a debtor can obtain a discharge which "discharges the debtor from all debts that arose before the date of the order for relief under this chapter . . . ."<sup>1</sup> In Chapter 13, a debtor receives a discharge after the debtor has made all payments under a Chapter 13 plan.<sup>2</sup> Similarly, in an individual Chapter 11 proceeding, a debtor obtains a discharge from the court only upon completion of all plan payments.<sup>3</sup>

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<sup>1</sup> 11. U.S.C. § 727(b).

<sup>2</sup> 11 U.S.C. § 1328(a).

<sup>3</sup> 11 U.S.C. § 1141(d)(5).

## THE DISCHARGE INJUNCTION

The Bankruptcy Code provides that a discharge: “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.”<sup>4</sup> Once a debtor obtains a discharge in bankruptcy, creditors can no longer seek to collect on debts that were discharged. This prohibition constitutes a permanent injunction as supported by the legislative history.<sup>5</sup> Once the discharge is entered, no debts that were discharged may be collected ever.<sup>6</sup>

## VIOLATIONS OF THE DISCHARGE INJUNCTION

Several courts have found creditors in contempt for violating the discharge injunction and have imposed monetary sanctions. For example, in *McLean v. Greenpoint Credit LLC*,<sup>7</sup> the debtors filed a Chapter 13 proceeding that was converted to a Chapter 7 proceeding where an order of discharge was entered. Several years later, when the debtors filed a new Chapter 13 petition, one creditor filed a claim seeking payment on account of the same debt that had been discharged in the previous bankruptcy proceeding.<sup>8</sup> The debtors objected to the claim and filed an adversary proceeding (a lawsuit in the bankruptcy) seeking actual damages for emotional distress,<sup>9</sup> legal fees and punitive damages.<sup>10</sup> The bankruptcy court sustained the objection to the claim. The husband testified that the bankruptcy court sent him notice that his plan payments would double after the claim was filed and that he would not be able to complete the Chapter 13 plan.<sup>11</sup> The creditor’s representative admitted that the creditor had notice of the discharge but asserted that the filing of the claim was a computer error.<sup>12</sup>

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<sup>4</sup> 11 U.S.C. § 524(a)(2).

<sup>5</sup> *McLean v. Greenpoint Credit LLC*, 515 B.R. 841, 846 (M.D. Ala. 2014) (once debt is discharged, debtor will not be pressured in any way to repay it).

<sup>6</sup> *United States v. White*, 466 F.3d 1241, 1246 (11th Cir. 2006) (discharge injunction is permanent injunction against collection of debts).

<sup>7</sup> 515 B.R. at 844.

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

<sup>9</sup> The husband was a disabled veteran suffering from PTSD.

<sup>10</sup> *Id.* at 845.

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

<sup>12</sup> *Id.*

The district court affirmed the bankruptcy court's holding that the creditor had violated the discharge injunction and the award of \$25,000 in actual damages, \$18,355.16 in attorneys' fees and sanctions in the amount of \$50,000.<sup>13</sup> First, the court concluded that filing a proof of claim is a violation of the discharge injunction which could subject a creditor to contempt sanctions if the violation was willful.<sup>14</sup> In this case, the court determined that there was a willful violation as the creditor admitted it had known of the discharge injunction.<sup>15</sup> Computer problems did not constitute a defense to the willful violation.<sup>16</sup> The court also concluded that, under Section 105 of the Bankruptcy Code,<sup>17</sup> emotional damages, monetary relief and punitive sanctions were proper.<sup>18</sup> "The discharge injunction is critical to the debtors' fresh start, and violations frustrate the goals of the bankruptcy code."<sup>19</sup>

*In the Matter of Hebner*<sup>20</sup> is another tale of caution for institutional lenders that violate the discharge injunction. Notwithstanding notice of the debtors' discharge, for three years Wells Fargo continued its collection efforts until the debtors filed a motion to hold the bank in contempt.<sup>21</sup> In addition to its continued collection efforts, Wells Fargo listed the debt associated with the debtors' former residence (that had been foreclosed upon) on credit reports.<sup>22</sup>

The court granted the debtors' motion for contempt and then ruled in the debtors' favor on the damages issue, awarding \$2,500 in actual damages, \$10,000 in punitive damages and actual attorneys' fees (in excess of \$23,000).<sup>23</sup> The court noted that the discharge injunction operates as a permanent injunction that replaces the automatic stay in bankruptcy.<sup>24</sup> The court believed

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<sup>13</sup> *Id.* at 851.

<sup>14</sup> *Id.* at 847.

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

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

<sup>17</sup> This section contains generic language allowing a bankruptcy court to enter any order or judgment necessary to carry out the provisions of the Bankruptcy Code. 11 U.S.C. § 105.

<sup>18</sup> 515 B.R. at 848. *See also In re Hardy*, 97 F.3d 1384, 1389 (11th Cir. 1996) (court can hold violating creditor in contempt and can award monetary damages).

<sup>19</sup> *Greenpoint Credit*, 515 B.R. at 851.

<sup>20</sup> Bankr. D. Neb. Jan, 8, 2015.

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

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

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

<sup>24</sup> *Id.* *See also Waswick v. Stutsman County Bank*, 212 B.R. 350, 352 (Bankr. D. N.D. 1997) (purpose of Section 542(a)(2) is to continue stay imposed by Section 362 when case is filed).

that a willful violation of the discharge injunction warrants a finding of civil contempt and the imposition of sanctions.<sup>25</sup> The court was less than impressed with Wells Fargo's practices and cautioned that: "Three years after entry of the bankruptcy discharge is more than sufficient time for Wells Fargo and its agents to stop the computer generated correspondence and put an end to the contact with the debtors that seem intended, openly or implicitly, to collect the balance owed to it."<sup>26</sup> The court concluded that Wells Fargo's "deliberate and repeated actions" damaged the debtors' ability to have a fresh start and therefore actual and punitive damages were warranted.<sup>27</sup>

In *In re Humphrey*,<sup>28</sup> the Chapter 7 debtors filed a motion for sanctions against Bank of America for violations of the discharge injunction. Inexplicably, Bank of America did not respond to the motion or show up at the hearing.<sup>29</sup> After the debtors received a discharge and their bankruptcy case was closed, they received 38 phone calls from Bank of America trying to collect the discharged debt.<sup>30</sup> When the debtors informed the Bank of America agents about the discharge they responded that "they did not care about the bankruptcy and the phone calls would not stop until the Debtors contacted the Bank of America bankruptcy department and until Bank of America updated its computer system."<sup>31</sup> Notwithstanding two subsequent cease and desist letters by debtors' counsel, Bank of America continued with the collection calls.<sup>32</sup>

Unsurprisingly, the court was not amused and concluded at a hearing that the debtors' "significant aggravation, emotional distress, and inconvenience are readily apparent and do not require the presentation of medical evidence."<sup>33</sup> The court applied Section 105 of the bankruptcy code to find bank of America in contempt for a willful violation of the discharge injunction.<sup>34</sup> The court noted that the creditor's subjective intent or beliefs are irrelevant.<sup>35</sup> The

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<sup>25</sup> *In the Matter of Hebner*.

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

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

<sup>28</sup> Bankr. M.D. Fla. March 14, 2012.

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

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

<sup>31</sup> *Id.*

<sup>32</sup> *Id.*

<sup>33</sup> *Id.*

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

<sup>35</sup> *Id.* See also *In re Hardy*, 97 F.3d at 1390 (creditor's subjective beliefs or intent are



“knowledge” part of the two part test (the other element is taking collection action) is satisfied by receipt of notice of the discharge.<sup>36</sup> To leave no doubt about its view of the lender’s actions, the court wrote: “Bank of America’s repeated failures to honor the discharge injunction were intentional, egregious and extreme. It acted with bad faith, its conduct was vexatious, wanton, and oppressive.”<sup>37</sup> The court awarded actual damages of \$12,500,000, including attorneys’ fees of \$2,500,000.<sup>38</sup> Surprisingly, in light of its highly critical comments, the court did not award punitive damages.

In yet another case where the debtor sued for an order of contempt for violating the discharge injunction, the lender failed to respond to show up at the hearing. In *In re Wassem*,<sup>39</sup> the court held an evidentiary hearing on the debtor’s motion for sanctions for violating the discharge injunction. The court found that the lender, Aurora Loan Services, LLC, had actual notice of the debtor’s discharge but thereafter made 44 telephone calls over a five month period seeking to collect the discharged debt, even after receiving notice of the sanctions motion.<sup>40</sup> The court found the lender to be in contempt of the discharge injunction and concluded that the lender had acted in bad faith.<sup>41</sup> Aurora’s repeated telephone calls were “vexatious, wanton, and oppressive. Aurora committed forty-four separate willful violations of the Debtor’s discharge injunction.”<sup>42</sup> The court awarded the debtor \$9,400 in actual damages, including \$5,000 in attorneys’ fees and awarded \$20,000 in punitive damages.<sup>43</sup>

## CONCLUSION

As can be seen in the above cases, it is advisable to pay attention to notices received when a borrower files for bankruptcy. Failing to adhere to, or simply

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irrelevant); *In re Caffey*, 384 B.R. 297, 307 (Bankr. S.D. Ala. 2008) (no specific intent requirement for willful violation).

<sup>36</sup> *Id.*

<sup>37</sup> *Id.*

<sup>38</sup> *Id.*

<sup>39</sup> 456 B.R. 566, 568 (Bankr. M.D. Fla. 2009).

<sup>40</sup> *Id.* at 569–70.

<sup>41</sup> *Id.* at 570.

<sup>42</sup> *Id.*

<sup>43</sup> *Id.* at 573. See also *In re Ashley* (Bankr. N.D. Ala. Sept. 6, 2012) (concluding that creditor’s continued collection actions despite knowledge of bankruptcy were deliberate and willful violations of discharge injunction and awarding sanctions in the amount of \$12,011,400, including \$5,000 in punitive damages).

ignoring, a notice of a discharge injunction can often lead to the imposition of sanctions, including punitive damages. These kinds of violations, even though not malicious in nature, are frequently deemed to be willful and can be easily avoided.