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2021 Consumer Practice Extravaganza

Taking Rule 3002.1 Sanctions Down the *Gravel* Road to Casa *Blanco*

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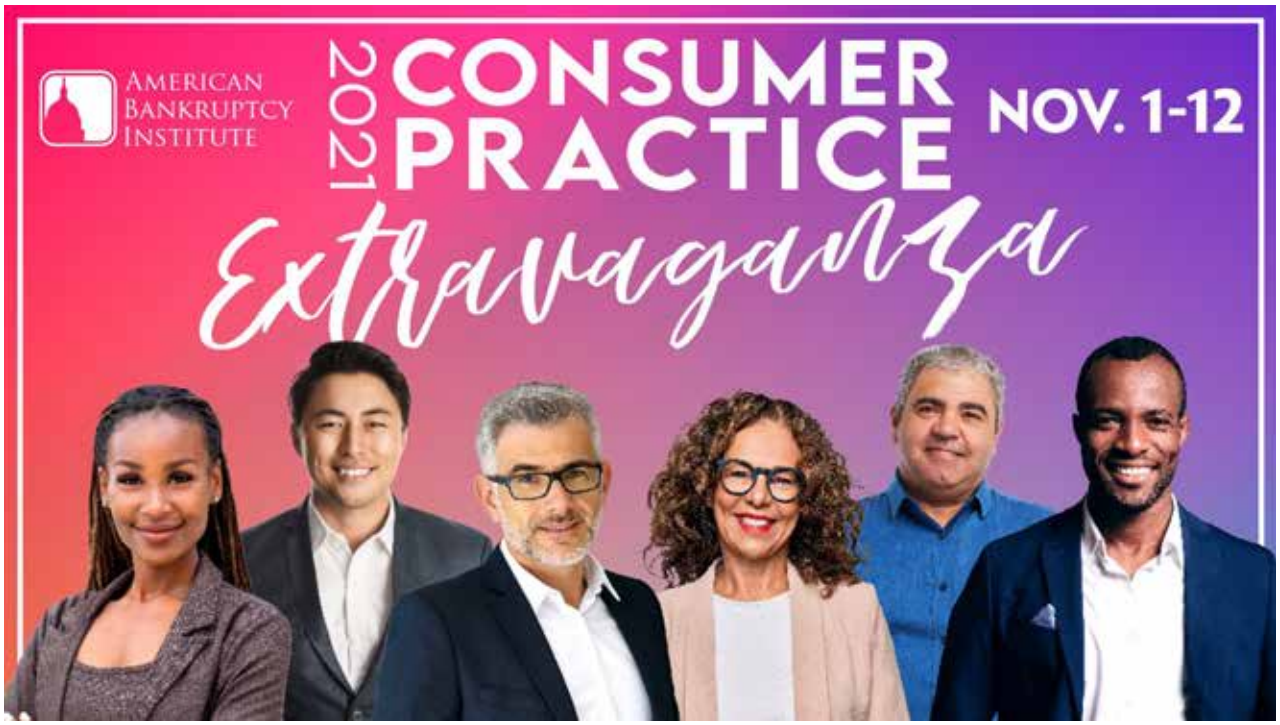
CONCURRENT SESSION

2021



From Taggart and the Old Ground to Hard Rocks and Gravel

The road to Hell may have been paved with good intentions but this is not the case for seeking punitive sanctions for a creditor's violation of various bankruptcy orders and enforcement rules. If there was ever any fair ground for doubt about where the Circuit Courts and the Supreme Court are headed, then you must understand the twists and turns of the road from Taggart to Gravel. In short, the Federal Appellate Courts have created what should be clear and willful contempt of court violations into simple rule enforcement cases. The objective of this webinar is to provide guidance on how to create a solid factual record that will allow the bankruptcy court to properly exercise its power of contempt, including punitive sanctions. In fact, the Court of Appeals in Gravel noted that "[t]he bankruptcy court could have crafted an order that would have forbidden the conduct troubling the Trustee."

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- Bankruptcy Rule 3002.1 went into effect on December 1, 2011.
- It was intended to provide greater transparency to debtors, trustees, and bankruptcy courts regarding debtors' ongoing mortgage payment obligations in Chapter 13 bankruptcy proceedings.

- Rule 3002.1 applies "in a Chapter 13 case to claims":
  - (1) that are secured by a security interest in the debtor's principal residence, and
  - (2) for which the plan provides that either the trustee or the debtor will make contractual installment payments."
- "Unless the court orders otherwise, the notice requirements of these Rules cease to apply when an order terminating or annulling the automatic stay becomes effective."

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Three types of filings required by Rule 3002.1:

- Notice of Mortgage Payment Change (subsection (b)).
- Notices of Fees, Expenses and Charges (subsection (c)).
- Responses to Notice of Final Cure Payments (subsection (g)).

- The national Bankruptcy Rules do not require a "motion to deem current" at the end of a "cure and maintain" Chapter 13 case, but some Local Rules require them.

- Additionally, an Order entered by the Bankruptcy Court pursuant to a motion filed under subsection (h) in response to a creditor's response under subsection (g) to the Trustee's notice of final cure under subsection (f) could deem the mortgage loan current and have additional provisions.

    - ". . . The court shall . . . determine whether the debtor has cured the default and paid all required postpetition amounts."

- Second Circuit's Gravel Opinion Reversed Awards of Sanctions by Bankruptcy Court Pursuant to Contempt Power **and** Sanctions for Violation of Rule 3002.1's Requirements

- Bankruptcy Court's contempt sanctions were based on Bankruptcy Court's finding that servicer violated deem current order entered upon completion of debtors' Chapter 13 plans

- The Rule 3002.1 sanctions were awarded for each instance of mortgage servicer's listing of undisclosed post-petition fees that the servicer included on post-discharge mortgage statements.

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- Rule 3002.1 Notices of Fees, Expenses and Charges (subsection (c) and (e)) were involved in *Gravel*.
  - "The holder of the claim shall file and serve on the debtor, debtor's counsel, and the trustee a notice itemizing all fees, expenses, or charges (1) that were incurred in connection with the claim after the bankruptcy case was filed, and (2) that the holder asserts are recoverable against the debtor or against the debtor's principal residence." (subsection (c)).
  - "The notice shall be served within 180 days after the date on which the fees, expenses, or charges are incurred." (subsection (c)).
  - "On motion of a party in interest filed within one year after service of a notice under subdivision (c) of this rule, the court shall, after notice and hearing, determine whether payment of any claimed fee, expense, or charge is required by the underlying agreement and applicable nonbankruptcy law to cure a default or maintain payments in accordance with § 1322(b)(5) of the Code." (subsection (e)).

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- Rule 3002.1's Penalty Provision – Subsection (i) ("Failure to Notify").
- "If the holder of a claim **fails to provide any information** as required by subdivision (b), (c), or (g) of this rule, the court may, after notice and hearing, take either or both of the following actions:
  - (1) preclude the holder from presenting the omitted information, in any form, as evidence in any contested matter or adversary proceeding in the case, unless the court determines that the failure was substantially justified or is harmless; or
  - (2) **award other appropriate relief**, including reasonable expenses and attorney's fees caused by the failure."

Case Law Split on whether Rule 3002.1(i) Applies to ***incorrect*** Rule 3002.1(b) and (c) notices (as opposed to sanctions for failure to file the notices):

- *In re Ferrell*, 580 B.R. 181, 188 (Bankr. D.S.C. 2017)
  - "For these reasons, the Court finds that it is appropriate to treat Shellpoint's inaccurate Supplement as the equivalent of a failure to provide the information required by Bankruptcy Rule 3002.1(g), thus subjecting Shellpoint to sanctions pursuant to Bankruptcy Rule 3002.1(i) and § 105."
- *In re Trevino*, 615 B.R. 108, 146 (Bankr. S.D. Tex. 2020)
  - "Because Rule 3002.1(i) provides relief in situations involving a lack of notice, rather than incorrect notice, the Court finds that it should deny Plaintiffs' request to award reasonable and necessary fees and expenses under Rule 3002.1(i)."

- *In re Gravel*, 6 F.4th 503 (2nd Cir. August 2, 2021).
- It was a 2-1 panel decision (motion for *en banc* rehearing denied Nov. 1, 2021)
- Involved the Chapter 13 Trustee's motions for contempt and sanctions in three separate debtor Chapter 13 cases.
- Several trade groups and six retired BK Judges filed amicus briefs in support of the Chapter 13 Trustee's motion for rehearing (and also in the main appeal).

- *Gravel* involved long-running litigation over $716 of unnoticed fees servicer assessed to three Chapter 13 debtors' mortgage accounts during their Chapter 13 bankruptcy cases, which servicer listed on monthly statements after the borrower had successfully completed a Chapter 13 "cure and maintain" case.

- Prior to the litigation at issue, the servicer in 2014 settled the Trustee's motion to compel and for sanctions with respect to unnoticed late fees on two monthly statements and a foreclosure threat for $9K.

- The late fees were incurred because the servicer had not taken into account the local practice of a two-month "gap" claim for the first two post-petition payments, which were paid in full over the plan like an arrearage claim.

- The Trustee had written to the servicer on two occasions prior to filing her motion but had not received a response.

- The Gravels successfully finished their "cure and maintain" Chapter 13 case in 2016 and a "deem current" order was entered stating that they were current on their mortgage payments.

- The **Trustee** subsequently discovered in a monthly statement that the servicer had been assessing property inspections fees in connection with the borrower's loan, which as of date of the statement had grown to $258.75, without filing a Rule 3002.1(c) notice for them.

- The Trustee also learned that in another Chapter 13 case (Beaulieu) the same servicer had assessed an NSF fee of $30 and property inspection fees of $56.25 which had appeared on monthly statements during the Chapter 13 and the first statement sent after a similar "deem current" order entered after the debtors successfully completed their Chapter 13 case without filing a Rule 3002.1(c) notice.

- Finally, the Trustee learned that the same servicer had assessed a late charge of $124.50 and property inspection fee of $246.50, both of which appeared on monthly statements during another Chapter 13 case (Kinsley), again without filing Rule 3002.1(c) notice.

- The Trustee filed motions for contempt for violation of the "deem current" orders in the Gravel and Beaulieu cases, and a motion for sanctions under Rule 3002.1(i) in all three cases.

- The Vermont BK Court entered sanctions $200K in Gravel and $100K in Beaulieu for contempt of the "deem current" orders at the ends of those cases.

- The Vermont BK Court also entered sanctions of $25K in each of the three cases based on a $1K amount for each of the 25 monthly statements in the three cases that included fees that were not noticed under Rule 3002.1(i).

- This decision is reported at *In re Gravel*, 556 B.R. 561 (Bankr. D. Vt. 2016).

- The Vermont District Court reversed and remanded the Vermont BK Court. *In re Gravel*, 6999820, at *1 (D. Vt. Dec. 18, 2017).

- District Court held that Bankruptcy Court's sanctions were in the nature of criminal contempt sanctions and the Bankruptcy Court lacked constitutional authority to award such sanctions as a non-Article III court.

- On remand, the Vermont Bankruptcy Court reduced its awards for violation of the "deem current" orders collectively from $200K to $150K in Gravel and from $100K to $75K in Beaulieu but kept the $25K per case sanctions for violation of Rule 3002.1(c). *In re Gravel*, 601 B.R. 873 (Bankr. D. Vt. 2019).

- Pursuant to the Trustee's request, the BK Court then certified the proceedings for direct appeal to the 2nd Circuit, which accepted the request.

- The Vermont BK Court certified 3 questions relating to the power of bankruptcy courts to:
  - (1) impose "punitive non-contempt sanctions" under Rule 3002.1.
  - (2) impose such sanctions under § 105(a).
  - (3) impose them "commensurate (in amount) to the violation at hand."
- The 2nd Circuit, however, noted that a direct appeal involves "orders" and not questions.
- It nevertheless stated that it could answer the certified questions only insofar as they help resolve the questions of law raised in the issues on appeal:
  - (1) whether the bankruptcy court properly sanctioned PHH for violating the Current Orders
  - (2) whether the bankruptcy court properly sanctioned PHH for violating Rule 3002.1.

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- The 2nd Circuit initially addressed the sanctions for violation of the two "deem current" orders.
- It first rejected the Trustee's argument that the BK Court could enter "non-contempt-based sanctions."
- It held that the BK Court's "discretion to award sanctions may be exercised only on the basis of the specific authority invoked by that court," and that regardless the BK Court had clearly relied on its contempt powers in its ruling.

- The 2nd Circuit first addressed the sanctions for violation of the two "deem current" orders.
- It began with a cite to the USSC's 2019 decision in *Taggart*, which it found held that:
  - ". . . a bankruptcy court may hold a creditor in contempt for violating the court's injunction only 'if there is *no fair ground of doubt* as to whether the order barred the creditor's conduct.'"
- It then noted that this holding was based on two principles re-emphasized in *Taggart*:
  - "civil contempt is a severe remedy"
  - "basic fairness requires that those enjoined receive explicit notice of what conduct is outlawed."

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- The 2nd Circuit then noted that there were two operative phrases in the "deem current" orders:
  - (1) the language that the debtors were current on all of their mortgage payments.
  - (2) the language stating that ". . . the mortgagee [PHH] shall be precluded from disputing that the debtors are current (as set forth herein) in any other proceeding."
- CA2 held that the "deem current" language "does not in itself clearly forbid any conduct," and failed to describe an "act or acts restrained or required" – in other words, it was not an injunction. Here, servicer listed the charges on the statement, but did not include them in the total payment due section. Statement also included language indicating that it was not an attempt to collect.
- CA2 summarily held that as to the "other proceeding" language, "however broad" it may be, "there is fair ground of doubt as to whether it would reach PHH's out-of-court conduct in these proceedings."

- The 2nd Circuit then addressed the sanctions for violation of Rule 3002.1(c) for failure to file fee notices.
- It noted that the BK Court had invoked the "other appropriate relief" language in Rule 3002.1(i)(2) to award punitive sanctions.
- It noted that the issue was one of first impression, and that the BK Court appeared to have been the only court that had awarded punitive damages/sanctions under Rule 3002.1(i)(2).

- The 2nd Circuit first noted that Rule 3002.1(i)(1) includes specific examples of compensatory damages, whereas "other appropriate relief" was a general term.
- It then invoked the statutory construction that "other appropriate relief" is best construed in a fashion that limits it as general language to the same class of matters as specific relief found in Rule 3002.1(i), finding that all other forms of relief therein are compensatory or evidence preclusion which is like compensatory.
- It further noted that when punitive damages are recoverable under the Bankruptcy Code, they are specifically mentioned, citing section 362(k).

- The 2nd Circuit then turned to the dissent.
- It rejected the dissent's analogy to Federal Rule of Civil Procedure 37, under which some courts have issues punitive discovery sanctions, noting that Rule 3002.1(i) had no "just orders" provision like Rule 37 and that Rule 37 is designed to protect the integrity of the judicial process instead of the interest of the parties.
- It also rejected the dissent's (and the Trustee's) argument that punitive sanctions could be awarded under the BK Court's inherent powers.
    - It agreed that courts have inherent powers to impose "relatively minor compensatory sanctions."
    - But it found that the BK Court did not base its award on its inherent power, but rather specifically tied it to Rule 3002.1(i).
    - It also found that there must be a finding of bad faith to impose such sanctions, and strongly criticized the dissent for assuming there was bad faith without a specific finding by the BK Court.

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- The 2nd Circuit then pointed to two facts about the dispute which it appeared to emphasize:
    - While they unnoticed fees appeared on the monthly statements, payment of them were never demanded.
    - The fees totaled $716.
- It then concluded by making an important observation about the dissent's concern that its holding would "undoubtedly hamper the ability of bankruptcy courts" to deter violations and protect debtors:
    - "In any event, the majority opinion does not limit a bankruptcy court's inherent power to sanction offenders who act in bad faith. That is just not what the bankruptcy court did here; others might be free to do so if they were to make sufficient findings."

BLANCO

Blanco's 2011 Bankruptcy Case:

On August 1, 2011, the case was filed. Bayview filed a Proof of Claim for $124,157.54 and stated the loan was $16,052.69 in arrears.

Bayview stated in the Claim that the monthly mortgage payment was $1,197.00 and that the fixed interest rate was 5.525%.

The plan was confirmed with no objection to the Proof of Claim.

This was a Conduit Plan and thus the mortgage payment was included in the monthly plan payment.

Notice of Payment Change Under Rule 3002.1(b)(1):

On November 30, 2011, Bayview filed the NPC indicating that the payments would increase to $1,251.57 per month due to an escrow deficiency.

No objection was filed to the NPC.

On December 21, 2011 Bayview filed a MFRS indicating that the on-going mortgage payments were $1,197.40, not the increased payment of $1,251.57 per the approved NPC.

The MFRS was resolved by an Agreed Order that the payments were $1,197.40 and the Trustee changed retroactively the monthly payment on his report.

The Trustee's Rule 3002.1(f) Motion Deem the Mortgage Current:

On September 29, 2016, the Trustee filed a Motion to Deem the Mortgage Current under Federal Rule of Bankruptcy Procedure 3002.1(f).

Bayview responded on October 5, 2016 by Form 4100R and agreed with the Trustee that:

1. The Pre-Petition default was fully cured under the Plan;
2. The Debtors were current with all post-petition payments, including all fees, charges, expenses, escrow, and costs; and
3. The next mortgage payment was due on September 1, 2016.
4. Bayview did not object to the amount of the payment of $1,197.40.

The Deemed Current Order:

On October 11, 2016, the Court signed an Order Deeming Mortgage Current and Directing Debtors to Resume Payments ("Deem Current Order"). Under the Order, the court found that ALL payments to Bayview under the confirmed Plan were completed and that:

1. The Claims of the creditor were all deemed current;
2. All escrow deficiencies, if any, were deemed cured;
3. All legal fees, inspection fees and other charges imposed by the servicer, if any, are deemed satisfied in full as of the next payment due date;
4. The Servicer shall be solely responsible for any shortfall or failure to respond to the Trustee's notice and motion; and
5. The Blancos were to resume direct payments of $1,197.40 beginning in September of 2016.

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The Second Bankruptcy Case:

On February 27, 2020, the Blancos filed a second Chapter 13 case after growing frustrated with the billing and overbilling practices of Bayview and their inability to correct all of the issues.

They also filed to stop a foreclosure sale on August 6, 2019 that had been scheduled pursuant to a petition filed by Bayview.

Debtors admitted that they stopped making payments to Bayview on November of 2018 because of their frustration with the actions of Bayview.

Bayview filed an original Proof of Claim and amended the claim twice. The Second Amended Proof of claim provided:

a. Monthly mortgage payments in the amount of $1,453.39;
b. Outstanding principal of $103,483.49;
c. Default interest of $12,142.60;
d. Fees and costs due of $6,865.97;
e. Escrow deficiency funds of $3,212.69; and
f. Less total funds on hand of $355.37 (suspense)
g. Total debt $132,678.08

The Rule 3002.1 Claim:

Plaintiffs' Count III alleges that Defendant violated Federal Rule of Bankruptcy Procedure 3002.1(b) and (c). Plaintiffs allege that Defendant changed Plaintiffs' monthly mortgage payment three times—on September 1, 2013 to $1,276; on October 1, 2014 to $1,195; and on December 1, 2015 to $1,454—without filing the required Rule 3002.1(b) notice.

Plaintiffs also allege that Defendant violated Rule 3002.1(c) by assessing "BK Fees, Legal Fees or Costs, Property Inspection Fees, and Title Costs," during the 2011 Case without filing the correct notice.

The Servicer filed a Motion to Dismiss Count III of the Adversary Proceeding on the following grounds:

(a) as a procedural rule, Rule 3002.1 does not create a private cause of action;

(b) violations of Rule 3002.1 in a prior case cannot be brought in a subsequent unrelated adversarial proceeding;

(c) punitive sanctions are not permitted by Rule 3002.1(i)(2); and

(d) in the alternative , the debtors have failed to plead any harm for the alleged failures to comply with Rule 3002.1.

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The Court rejected the Count III arguments and held:

"The plain language of Rule 3002.1(i) provides that where "the holder of a claim fails to provide any information as required by subdivision (b), (c), or (g) of this rule, the court may, after notice and hearing . . . award other appropriate relief, including reasonable expenses and attorney's fees caused by the failure."

Rule 3002.1 lays out both the grounds of violation—failure to follow subdivision (b), (c), or (g)—and a remedy for such violations—appropriate relief.

*Even the advisory committee notes recognize that a Chapter 13 debtor who has made all plan payments and whose case has been closed may move to have the case reopened for the purpose of seeking sanctions under Rule 3002.1(i).217.

Nevertheless, this Court need not decide whether Rule 3002.1 creates an independent cause of action because Plaintiffs allege that Defendant violated Rule 3002.1(b) and (c) and subdivision (i)(2) permits this Court to award ". . . other appropriate relief, including reasonable expenses and attorney's fees. . ." for such violations. In Trevino, this Court held that although the plaintiffs there could have utilized a Rule 3002.1(e) contested matter to object to the defendants' 3002.1(c) notice, plaintiffs could also raise the objection in an adversary proceeding and in fact, must file an adversary proceeding when seeking to recover money or property.

Here, Plaintiffs seek an array of sanctions, including the recovery of money for Defendant's alleged violations of the Rule. Thus, it was appropriate for Plaintiffs to bring their Rule 3002.1 violations in this adversary proceeding.

Plaintiffs' Count III for Rule 3002.1 violations committed in the 2011 Case is appropriate in this case:

Defendant also argues that it is improper for Plaintiffs to seek damages for alleged violations of Rule 3002.1 occurring in the 2011 Case in a subsequent, unrelated adversary action. In support, Defendant points to the plain language of the Rule itself: "the court may . . . preclude the holder from presenting the omitted information, in any form, as evidence in any contested matter or adversary proceeding in the case[,]" which does not indicate that relief may be sought in a case other than the bankruptcy case in which the violation occurred.

Defendant also points to the Advisory Committee Notes of Rule 3002.1, which states:

If, after the chapter 13 debtor has completed payments under the plan and the case has been closed, the holder of a claim secured by the debtor's principal residence seeks to recover amounts that should have been but were not disclosed under this rule, the debtor may move to have the case reopened in order to seek sanctions against the holder of the claim under subdivision (i).

While the advisory committee note makes clear that a debtor may move to reopen a case to seek sanctions under Rule 3002.1(i), nothing in the note prevents a debtor from bringing a Rule 3002.1 violation in a subsequent case.

More importantly, this Court is unpersuaded that the plain language of Rule 3002.1 prevents a debtor from seeking "appropriate relief, including reasonable expenses and attorney's fees caused by the failure[,]" in a subsequent case.

The Rule expressly permits the court to preclude the claim holder from presenting omitted information in "the case" in subsection (i)(1), but the Rule is silent as to whether the court can award relief in a later case.

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Blanco Opinion's Discussion of the Second Circuit's Gravel Opinion (agreeing with the dissent):

The Gravel dissent concluded that the plain meaning of "other appropriate relief under Rule 3002.1, as confirmed by its modeling under Rule 37 and the purpose of the Rule, authorized bankruptcy courts in appropriate circumstances to impose sanctions for gross violations of Rule 3002.1. The dissent noted the plain language of the Rule by the use of the term "including" meant that under 11 USC 102(3) and (i)(2) the term should be interpreted to mean "including, but not limited to" compensatory relief.

The dissenting opinion in Gravel also compared Rule 3002.1 to FRCP 37(c)(1), after which the Rule was modeled. In relevant part, FRCP 37(c)(1) contains an evidence-preclusion sanction and states that if a party fails to adhere to FRCP 26(a) or (e), then the court:

"(A) may order payment of the reasonable expenses including attorney's fees, caused by the failure . . . and
(C) may impose other appropriate sanctions, including any of the orders listed in Rule 37(b)(2)(A)(i)-(vi)." And although the Second Circuit has never decided whether punitive damages can be assessed under FRCP 37, the dissent agreed with the majority of courts that they could be under the "other appropriate sanctions" language in the Rule.
Rule 3002.1(i)(2) contains the same "appropriate relief language, which operates as a catch-all provision in both Rules."
This language cloaks the Court with the flexibility and discretion to imposed unenumerated punitive sanctions, as noted.

Lastly, the dissent considered the purpose behind the enactment of Rule 3002.1.
Prior to Rule 3002.1, mortgagees, without notice to the debtor, would add fees and costs to the debtor's mortgage during the pendency of the bankruptcy case. After the bankruptcy case ended, mortgagees attempted to foreclose on debtors based on those post-petition defaults for which they assessed fees.

Rule 3002.1 was adopted to remedy that problem by requiring the mortgagee to give both the debtor and the trustee notice of fees and payment changes during the bankruptcy case.

To limit the remedies permitted under Rule 3002.1 to compensatory awards would likely render that provision an insufficient deterrent, where the fees assessed by mortgagees are often relatively small and either go unnoticed by debtors or debtors choose not to fight them. **Without the possibility of punitive damages, mortgagees have little incentive to make the systemic changes required to service loans in Chapter 13.**

The plain language of Rule 3002.1(i) and the policies underlying the Bankruptcy Code permit punitive damages and sanctions as "other appropriate relief" under Rule 3002.1(i)(2):

The plain language of Rule 3002.1 places few restrictions on the type of remedies bankruptcy courts can issue. First, under subdivision (i)(1), a court is only prohibited from precluding evidence if the creditor's failure was substantially justified and harmless. Second, under subdivision (i)(2), the relief the court can award is only limited to that which is "appropriate." Thus, the plain language of Rule 3002.1(i) provides courts significant latitude in awarding sanctions. Additionally, as discussed by the dissent in Gravel, the word "including," as used in the Rule, is not limiting. Reasonable expenses and attorney's fees are merely two examples, and not an exhaustive list. And the explicit mention of attorney's fees is necessary for courts to depart from the American Rule when considering fee shifting.

Permitting sanctions and punitive damages as "other appropriate relief" under Rule 3002.1(i)(2) also best serves the policy goals underlying the bankruptcy system. It is well recognized that a creditor's failure to comply with the notice requirements of Rule 3002.1 can hinder the honest debtor's right to a fresh start following bankruptcy. Punitive damages protect that right by deterring violations of the Rule that threaten a fresh start. Punitive damages could likewise curtail repeat bankruptcy filings, thereby conserving both judicial resources and the parties' resources. Where the debtor's fresh start is defiled by Rule 3002.1 violations, the likelihood of a subsequent bankruptcy filing is greater than zero.

*This case serves as a text-book example of the necessity for such damages and the extent to which Servicers simply fail to comply with the Bankruptcy Rules. If the majority of Chapter 13 cases fail, then why give a damn if the system is right or wrong!

Under the appropriate circumstances, courts may use punitive sanctions to curb opportunistic behavior. **As Kara Bruce explains in her article**:

Even if a consumer is aware that her rights have been violated, the damages available to that individual consumer are often too small to justify the costs of litigating a matter. These include not only direct costs (hiring an attorney and paying filing fees, for example), but also the time and effort it takes to locate an attorney, confirm that a legal claim exists, and commence suit. Even if a consumer can surmount these hurdles, the amount she is able to invest in a suit might well be dwarfed by the investment of a company that profits from perpetuating the harm on similarly situated consumers. These financial barriers to private litigation can theoretically be addressed by the imposition of litigation incentive, such as statutory or punitive damages, fee-shifting rules, and damage multipliers.

Plaintiffs have no duty to allege harm under Rule 3002.1(i):

In the alternative, Defendant moves to dismiss Plaintiffs' Count III on the basis that (1) Plaintiffs have not alleged that they suffered harm as a result of Defendant's alleged Rule 3002.1 violations; and (2) elimination of a lien or of any contractual obligations is not an appropriate remedy under Rule 3002.1(i)(2). Plaintiffs' Complaint seeks actual damages, attorneys' fees and costs, and any other appropriate relief, including substantial punitive damages and/or sanctions.

Additionally, Rule 3002.1. does not require Plaintiff to allege "harm" to be entitled to "other appropriate relief, including reasonable attorney fees." The court must provide notice and hearing, to preclude evidence the court must determine that the failure to comply caused harm and was not substantially justified, and other relief must be appropriate.

Accordingly, this Court finds that Rule 3002.1(i)(2) DOES NOT require Plaintiffs to plead harm and, even if it had, the Plaintiffs have more than met the burden in this case.

Jennifer Henderson
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JOSEPH F. BIANCO, *Circuit Judge*, concurring in part and dissenting in part:

I agree with the majority opinion that the Current Orders did not clearly and unambiguously prohibit PHH's conduct for which the bankruptcy court imposed the $225,000 sanction, and that the $225,000 should therefore be vacated. However, I respectfully part company with the majority opinion when it concludes that the bankruptcy court did not have the authority to impose $75,000 in sanctions under Federal Rule of Bankruptcy Procedure 3002.1 (the "Rule"), and that the bankruptcy court did not sufficiently invoke its inherent powers so as to allow this Court to separately review the $75,000 sanction under such powers.

As set forth below, the "other appropriate relief" language in the sanctions authority conferred upon bankruptcy courts under Rule 3002.1(i) provided a proper basis to impose the $75,000 punitive sanction against PHH based upon its flagrant and repeated violations of the Rule (as found by the bankruptcy court). Such an interpretation of the Rule is not only consistent with the plain text of the Rule itself but is further supported by the purpose of the Rule and the fact that the Rule was modeled after Rule 37 of the Federal Rules of Civil Procedure, which allows for similar punitive sanctions. In holding otherwise in the face of the broad language and purpose of the sanctions provision, the majority renders a

bankruptcy court powerless to levy *any sanction* under the Rule against a serial violator of the Rule's provisions over a substantial period of time where those violations (due to the diligence of the Trustee in identifying and rectifying the violations) did not result in any actual economic harm to the multiple debtors who were the victims of the Rule violations. In other words, in this case the majority concludes that the sanctions provision of the Rule does not allow the bankruptcy court to punish the misconduct of one of the largest subservicers of residential mortgages in the United States, even where a prior sanction was ineffective at achieving compliance. This interpretation will undoubtedly hamper the ability of bankruptcy courts, through their enforcement of this Rule, to provide deterrence and to protect debtors from predatory practices that interfere with the "fresh start" for debtors that is a fundamental purpose of bankruptcy protection under Chapter 13.

I also separately conclude that, even assuming *arguendo* such authority does not exist under the Rule itself, the bankruptcy court possessed the independent authority under its inherent powers to impose this $75,000 sanction against PHH for its egregious conduct in violation of the Rule. The majority holds that the bankruptcy court, in imposing sanctions for this misconduct, only "alluded" to its

inherent powers and did not provide sufficient reasoning to allow this Court to analyze the potential application of that power to the facts here. I respectfully disagree.

The bankruptcy court's explicit invocation of its inherent powers in both its order and its separate opinion, as well as its detailed reasoning regarding PHH's violations of the Rule and its thorough analysis of the "inherent powers" case authority relating to the sanction amount, together provided a more than sufficient record for us to hold that the imposition of the $75,000 sanction under such inherent powers was not an abuse of discretion. Moreover, although the majority suggests that it is "dubious" that a bankruptcy court can invoke its inherent powers in the absence of an explicit finding of bad faith, the Supreme Court and this Court have made clear that conduct that is "tantamount to bad faith" can provide the requisite factual predicate for imposing sanctions under a court's inherent powers, and I conclude that the bankruptcy court's findings satisfied that standard. This precedent regarding a district court's inherent powers to sanction in such situations applies with equal force to a bankruptcy court, which likewise has a correspondingly clear and compelling need to use such powers to vindicate its authority and ensure basic compliance with its rules and procedures.

In sum, I conclude that the bankruptcy court had the authority under Rule 3002.1(i), as well as its inherent powers, to sanction PHH for its repeated violations of the Rule, and did not abuse its discretion in setting the amount at $75,000 given the nature and scope of the violations by this multi-billion dollar company and the bankruptcy court's prior warning and sanction, as well as PHH's violation of its own commitment to rectify whatever lack of internal controls were causing these repeated violations.

I therefore join in the opinion of the majority, except with respect to Part D.

DISCUSSION

A. The Bankruptcy Court's Finding Regarding PHH's Pattern of Sanctionable Misconduct

Before reviewing the bankruptcy court's authority to impose sanctions for violations of Rule 3002.1 and the framework for exercising its discretion in determining the amount of such sanctions, it is necessary to briefly summarize the nature of PHH's repeated violations of the Rule, as found by the bankruptcy court (whose findings as to these violations are not disputed on appeal). This summary of the factual findings highlights that PHH's pattern of violations is precisely the type of conduct that the rule-makers sought to prevent, through the enactment of

the Rule and the accompanying sanctions provision that gives a bankruptcy court the ability to enforce the Rule and deter such conduct.

In this action, PHH sent the Gravels incorrect mortgage statements for two-and-one-half years from 2011 until 2014. In order to attempt to correct the misapplication of payments, the Trustee mailed multiple letters attaching detailed spreadsheets directly to PHH, in addition to filing the letters with the bankruptcy court so they would be sent to PHH's counsel via ECF. Receiving no response from PHH, the Trustee filed a motion for sanctions in the amount of a little over $12,000. Only in response to that motion did PHH acknowledge its error and indicate that it had implemented new remedial processes to prevent future accounting errors. At oral argument on that motion, PHH's counsel acknowledged to the bankruptcy court that it "obviously has the authority to offer sanctions." Joint App'x at 734. However, PHH's counsel averred that the sanctions motion had successfully brought this accounting problem to PHH's attention, and asked that the amount of any monetary sanctions be modest in light of PHH's response. In particular, PHH's counsel told the bankruptcy court that PHH had "taken remedial steps" and had "corrected the underlying problem." *Id.* at 724. PHH's counsel further explained, "[i]f [PHH has] problems again, they are

not going to have – they are not going to have that excuse. They are not going to have that defense." *Id.* Although the bankruptcy court expressed concerns about whether using progressive sanctions would curb the misconduct in a timely fashion, the bankruptcy court ultimately agreed to the amount of $9,000, which had been negotiated by PHH's counsel and the Trustee.

At least one other bankruptcy court had similarly warned PHH about its violation of Rule 3002.1. Specifically, in *In re Owens*, No. 12-40716, 2014 WL 184781 (Bankr. W.D.N.C. Jan. 15, 2014), a bankruptcy court found that PHH violated Rule 3002.1(c) when it sent debtors statements including post-petition fees that were more than 180 days old, without filing or serving the required Rule 3002.1(c) notice. The bankruptcy court specifically held that PHH must comply with Rule 3002.1(c), regardless of whether it actually intended to recover the fees. *Id.* at *4. The *Owens* court declined to sanction PHH under 3002.1(i) because the decision was rendered so soon after the Rule's effective date. *Id.* However, in that decision, the bankruptcy court unequivocally cautioned PHH that it "[might] consider awarding relief as against PHH under Rule 3002.1(i) should [the issue] come up in the future." *Id.*

Notwithstanding the prior sanction and warnings by bankruptcy courts about these violations, PHH's violations continued. More specifically, after orders were issued in the *Gravel* and *Beaulieu* actions, each of which attested that "the debtors have cured any mortgage arrearage or default" and were "current," Joint App'x at 705–06, 709, PHH sent twenty-five mortgage statements showing late charges and property inspection fees in both actions. PHH did the same in the *Knisley* action. Again, the Trustee filed motions for contempt and sanctions (this time in each action), and again, PHH waived the fees and removed them from the debtors' accounts. Only this time, in the exact reverse of its prior stance, PHH argued that motion practice was unnecessary, and that it would have happily removed the fees if the Trustee had only contacted PHH advising PHH of its error.

Among other sanctions, the bankruptcy court assessed a $1,000 sanction per violation of Rule 3002.1, for a total of $75,000 across all three actions, against PHH under Rule 3002.1(i) and its inherent powers.

B. Sanctions Under Federal Rule of Bankruptcy Procedure 3002.1(i)

I respectfully dissent from the majority's conclusion that Rule 3002.1 does not provide a bankruptcy court with the authority to impose sanctions. The plain meaning of the Rule, as bolstered by its purpose and a review of analogous rules,

supports the bankruptcy court's conclusion that Rule 3002.1(i)'s enforcement measures for violations of Rule 3002.1(c) include punitive monetary sanctions.

At the start, in support of its conclusion, the majority cites to a bankruptcy case, in which the bankruptcy court determined that it lacked the power to impose punitive sanctions under Rule 3002.1. *See In re Tollstrup*, No. 15-33924, 2018 WL 1384378, at *5 (Bankr. D. Or. Mar. 16, 2018). However, it also should be noted that other bankruptcy courts have reached a contrary conclusion. For example, a bankruptcy court recently allowed a claim for punitive sanctions under Rule 3002.1(i) to survive a motion to dismiss. *See In re Bivens*, 625 B.R. 843, 850–51 (Bankr. M.D.N.C. 2021); *see also In re Owens*, 2014 WL 184781, at *4 (warning PHH that the bankruptcy court would consider imposing sanctions under Rule 3002.1(i) if there were future violations). Thus, not only has no circuit court addressed this issue, but bankruptcy courts themselves are not in agreement.

"[T]he starting point in any case of interpretation must always be the language itself, giving effect to the plain meaning thereof." *Ret. Bd. of the Policemen's Annuity and Benefit Fund of the City of Chi. v. Bank of N.Y. Mellon*, 775 F.3d 154, 165 (2d Cir. 2014) (alteration in original) (internal quotation marks omitted). As set forth by the majority, Rule 3002.1(i) provides that:

> the court may, after notice and hearing, take either or both of the following actions: (1) preclude the holder from presenting the omitted information, in any form, as evidence in any contested matter or adversary proceeding in the case, unless the court determines that the failure was substantially justified or is harmless; or (2) award *other appropriate relief*, *including* reasonable expenses and attorney's fees caused by the failure.

Fed. R. Bankr. P. 3002.1(i) (emphasis added).

The Bankruptcy Code instructs that "'includes' and 'including' are not limiting[.]" 11 U.S.C. § 102(3). In essence, the Rule should be interpreted to mean "including, but not limited to," when enunciating the list of possible other relief that is available to the bankruptcy court. Therefore, the text is intended to be expansive: "[R]easonable expenses and attorney's fees" are but two possible types of "appropriate relief" within this sanctions provision. Fed. R. Bankr. P. 3002.1(i).

Notwithstanding this expansive language, the majority limits the Rule to allowing only non-punitive sanctions because, in its view, "reasonable expenses and attorney's fees" are both forms of compensatory relief and, when a statute provides specific examples, it is best to limit the general language to the same type of matters as those illustrated. Maj. Op. at 24–25 (quoting *Canada Life Assurance Co. v. Converium Ruckversicherung (Deutschland) AG*, 335 F.3d 52, 58 (2d Cir. 2003)). The use of that canon of construction, however, does not withstand closer scrutiny

when the phrase "other appropriate relief" is analyzed in the context of this particular sanctions provision.

As a threshold matter, one should not overlook the fact that Rule 3002.1(i) does not purport to be a subsection that focuses on compensatory relief. It is, at its core, a sanctions provision. In fact, as one bankruptcy court has articulated, "[i]n case the importance of complying with Rule 3002.1(c) is for some reason lost on a lender, Rule 3002.1(i) serves as a sobering reminder. It authorizes the court to punish the offending lender." *In re Lescinskas*, 628 B.R. 377, 382 (Bankr. D. Mass. 2021) (noting that the advisory committee notes to the 2011 adoption of the Rule described "subdivision (i) penalties as 'sanctions'"). Thus, this is not a situation where a bankruptcy court chose to impose punitive monetary sanctions under a provision that had nothing to do with sanctions.

The majority nevertheless seeks to cabin the bankruptcy court's authority to impose punitive sanctions under the broad phrase "other appropriate relief," *within this sanctions provision*, by asserting that the other enumerated sanctions under both Rule 3002.1(i)(1) and (2) are non-punitive (or compensatory) forms of sanctions. I respectfully disagree with that analysis. In particular, I do not accept the majority's classification of Rule 3002.1(i)(1) – namely, the evidence-preclusion

provision – as a non-punitive sanction. Although it does allow the violator to avoid the sanction if the failure to provide the requisite notice was harmless, it also allows for the imposition of the drastic sanction of exclusion regardless of the precise nature or amount of such harm. In other words, the sanction is not required to be proportionate to the harm – *i.e.*, compensatory in nature – but rather seeks to punish with the broad brush of evidence-preclusion to deter such violations in the future. Indeed, we have noted that in other contexts the preclusion of evidence can be a *more extreme* sanction than monetary sanctions. *See Cine Forty-Second St. Theatre Corp. v. Allied Artists Pictures Corp.*, 602 F.2d 1062, 1066 (2d Cir. 1979) (Rule 37 "provides a spectrum of sanctions. The mildest is an order to reimburse the opposing party for expenses caused by the failure to cooperate. More stringent are orders . . . prohibiting the introduction of evidence . . . . Preclusionary orders ensure that a party will not be able to profit from its own failure to comply. . . . [C]ourts are free to consider the general deterrent effect their orders may have on the instant case and on other litigation, provided that the party on whom they are imposed is, in some sense, at fault." (footnote and citations omitted)).

In fact, in the context of the evidence-exclusion sanction under Rule 37, we have explained the importance of the punitive nature of such a sanction as a deterrent to future violations. *See Daval Steel Prods. v. M/V Fakredine*, 951 F.2d 1357, 1365–67 (2d Cir. 1991) (discussing the district court's discretion to preclude evidence under Rule 37 and explaining that "[a]lthough an order granting a claim and precluding a party from presenting evidence in opposition to it is strong medicine, such orders are necessary on appropriate occasion to enforce compliance with the discovery rules and maintain a credible deterrent to potential violators"); *see also Nat'l Hockey League v. Metro. Hockey Club*, 427 U.S. 639, 643 (1976) (explaining Rule 37 sanctions must be applied diligently both "to penalize those whose conduct may be deemed to warrant such a sanction, [and] to deter those who might be tempted to such conduct in the absence of such a deterrent").

Once the evidence-preclusion penalty in Rule 3002.1(i)(1) is properly classified as a potentially punitive sanction that also operates as a deterrent, then the "other appropriate relief" language in Rule 3002.1(i)(2) naturally includes, from a textual standpoint, punitive monetary sanctions because they are part of "the same class of matters" contained within the related penalty provision. *Canada Life Assurance Co.*, 335 F.3d at 58.

This interpretation of the plain text of Rule 3002.1 to allow for punitive, non-compensatory sanctions is consistent with the Rule's purpose, as well as its origin and its amendment. As noted above, Rule 3002.1 was based on Federal Rule of Civil Procedure 37(c)(1).[1] This is also true of Federal Rule of Bankruptcy Procedure 3001(c)(2)(D), which is a companion rule to Rule 3002.1 and likewise addresses the failure of a holder of a claim to provide required information as part of a proof of claim and contains an identically-worded sanctions provision.[2] *See*

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[1] Rule 37(c)(1) states:

> If a party fails to provide information or identify a witness as required by Rule 26(a) or (e), the party is not allowed to use that information or witness to supply evidence on a motion, at a hearing, or at a trial, unless the failure was substantially justified or is harmless. In addition to or instead of this sanction, the court, on motion and after giving an opportunity to be heard:
>
> > (A) may order payment of the *reasonable expenses*, *including attorney's fees*, caused by the failure;
> >
> > (B) may inform the jury of the party's failure; and
> >
> > (C) may impose *other appropriate sanctions*, *including* any of the orders listed in Rule 37(b)(2)(A)(i)-(vi).

Fed. R. Civ. P. 37(c)(1) (emphases added).

[2] Rule 3001(c) states:

Advisory Comm. on Bankr. Rules, Subcomm. on Consumer Issues, Memorandum on Comments on Proposed Amendments to Rule 3001(c) and Proposed New Rule 3002.1, 12 (PDF page 63) (Apr. 7, 2010) ("The proposed sanctions [in Rule 3001(c)(2)(D)] most closely resemble the sanction available under Civil Rule 37(c)(1) for the failure to provide information required under the disclosure provisions of Rule 26(a)."), https://www.uscourts.gov/sites/default/files/fr_import/BK2010-04.pdf.

As the bankruptcy court noted below, district courts have concluded that the similar language of Rule 37 allows for the imposition of punitive, non-compensatory sanctions for violation of the discovery rules. *In re Gravel* ("*Gravel II*"), 601 B.R. 873, 886 (Bankr. D. Vt. 2019) (collecting cases). Although we have

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> If the holder of a claim fails to provide any information required by this subdivision (c), the court may, after notice and hearing, take either or both of the following actions:
>
> > (i) preclude the holder from presenting the omitted information, in any form, as evidence in any contested matter or adversary proceeding in the case, unless the court determines that the failure was substantially justified or is harmless; or
> >
> > (ii) *award other appropriate relief, including reasonable expenses and attorney's fees* caused by the failure.

Fed. R. Bankr. P. 3001(c)(2)(D) (emphasis added).

never decided this issue, I agree with the overwhelming majority of courts that have concluded such authority exists under Rule 37. *See, e.g.*, *Olivarez v. GEO Grp., Inc.*, 844 F.3d 200, 203 (5th Cir. 2016) ("Pursuant to Rule 37[(c)(1)] and the court's inherent authority, the district court imposed sanctions requiring each Appellant to pay a $1,000 fine."); *see also Nycomed U.S. Inc. v. Glenmark Generics Ltd.*, No. 08–CV–5023 (CBA)(RLM), 2010 WL 3173785, at *3, 11 (E.D.N.Y. Aug. 11, 2010) (imposing a non-compensatory fine of $25,000 and stating "[a] court may . . . levy monetary sanctions against a violating party in lieu of or *in addition to* the sanctions outlined in Rule 37(b)(2)(A)." (emphasis added)); *Danis v. USN Commc'ns, Inc.*, No. 98 C 7482, 2000 WL 1694325, at *51 (N.D. Ill. Oct. 23, 2000) (ordering the defendant to pay $10,000 fine under Rule 37(b)(2) and noting that, "[w]hile the imposition of a fine is not one of the sanctions specifically enumerated in Rule 37(b)(2), the language of Rule 37(b)(2) makes it clear that the enumerated sanctions are 'among others' that a Court may enter, and that they are therefore not intended to be exclusive"); *Winters v. Textron, Inc.*, 187 F.R.D. 518, 521–22 (M.D. Pa. 1999) (defendant ordered to pay $10,000 fine); *Miltope Corp. v. Hartford Cas. Ins. Co.*, 163 F.R.D. 191, 195 (S.D.N.Y. 1995) (plaintiff fined $1,000); *see generally* 8B Charles Alan

Wright et al., Federal Practice and Procedure § 2284 (3d ed. 2021) (sanctions enumerated in Rule 37 are not intended to be exclusive).

The majority nevertheless concludes that Rule 37 (and a lower court's use of that Rule to impose non-compensatory punitive sanctions) does not provide helpful guidance as to the intended scope of Bankruptcy Rule 3002.1 and, by extension, Rule 3001(c). In particular, in distinguishing these non-compensatory sanctions under Rule 37, the majority notes that "Rule 3002.1 lacks the authorization of 'just' orders" like that contained in Rule 37. Maj. Op. at 28 (quoting Fed. R. Civ. P. 37 (b)(2)(A)). However, the "just orders" clause, similar to the "other appropriate relief" catch-all provision at issue here, does not enumerate punitive monetary sanctions among its list of illustrative sanctions. In order to ensure compliance, both provisions use similar language to cloak the court with the flexibility and discretion to impose unenumerated punitive sanctions, regardless of whether such additional sanctions are characterized as "just orders" under Rule 37 or "other appropriate relief" under Rule 3002.1.

The majority also seeks to cast aside the analogous Rule 37 language and framework because unlike the "tailored enforcement mechanism" of Rule 3002.1, "[d]iscovery sanctions under Federal Rule 37 are deterrents (specific and general)

meant to punish a recalcitrant or evasive party" and "Federal Rule 37 protects more than the interest of a party in remedying or avoiding certain costs; it protects the interests of the parties, the court, and the public in a speedy and just resolution of the case." Maj. Op. at 26–27.

However, I find no daylight between the deterrent purpose of the sanctions provisions in Bankruptcy Rules 3002.1 and 3001(c) and the identical purpose of Rule 37, upon whose language they were modeled. Prior to the adoption of Rule 3002.1, "mortgage companies applied fees and costs to a debtor's mortgage while the debtor was in bankruptcy without giving notice to the debtor and then, based on these post-petition defaults, sought to foreclose upon the debtor's property after the debtor completed the plan." *In re Tollios*, 491 B.R. 886, 888 (Bankr. N.D. Ill. 2013). In response to that problematic practice, and after the financial crisis, Rule 3002.1 was adopted in December 2011 to ensure that both debtor and trustee were informed of the exact amount needed to cure any pre-petition arrearage and were furnished with notice of any changes in post-petition obligations. *See* Fed. R. Bankr. P. 3002.1 advisory committee notes to the 2011 adoption.

Importantly, the evidentiary exclusion was already in Rule 3001 before the adoption of Rules 3001(c) and 3002.1, which now provide additional sanctions,

including "other appropriate relief." As the bankruptcy court explained, this broadening of the available sanctions was a recognition that, in practice, "[t]here are many instances in which the evidentiary exclusion remedy provides little, if any, relief in the context of Rule 3001(c) and Rule 3002.1 sanctions motions." *Gravel II*, 601 B.R. at 885–86 (collecting cases). Additionally, another court has explained that "there can be no proceeding in which the evidentiary penalty of Rule 3001(c)(2)(D) could come into play" because "the chapter 13 plan has been fully administered." *In re Davenport*, 544 B.R. 245, 250 (Bankr. D.D.C. 2015); *see also In re Reynolds*, No. 11-30984, 2012 WL 3133489, at *3 (Bankr. D. Colo. July 31, 2012) ("At a hearing where the merits of a claim are not at issue, the penalty set out in Rule 3001(c)(2)(D) is meaningless because it only comes [into] play at a hearing on the merits of a claim where a court would otherwise entertain the type of evidence required by Rule 3001(c)(1).").

Thus, there is no doubt that the expansion of the sanctions, to include "other appropriate relief," was an effort to bring greater compliance under this Rule in the industry through the deterrence that such additional punitive sanctions would bring. *Cf.* Advisory Comm. on Bankr. Rules, Subcomm. on Consumer Issues, Memorandum on Comments on Proposed Amendments to Rule 3001(c) and

Proposed New Rule 3002.1, 12 (PDF page 63) (Apr. 7, 2010) ("The proposed addition of Rule 3001(c)(2)(D) was based on the Advisory Committee's belief that stronger sanctions are required to ensure greater compliance with the rule's requirements."), https://www.uscourts.gov/sites/default/files/fr_import/BK2010-04.pdf.

Bankruptcy courts have highlighted the importance of using these sanctions to achieve greater deterrence and, therefore, greater compliance under Rule 3002.1. *See In re Lescinskas*, 628 B.R. at 382, n.8 ("The gravity of Rule 3002.1 compliance was recently underscored by a series of multimillion dollar penalties negotiated by the Department of Justice's U.S. Trustee Program with certain national banks which the USTP had accused of, among other things, repeatedly violating Rule 3002.1."). For instance, in *Lescinskas*, the bankruptcy court disallowed *the bank's* contractual claim for attorney's fees and costs under Rule 3002.1(i)(2) even though such a sanction was punitive rather than compensatory and would result in a windfall for the debtor. *See id*. at 384 ("A legitimate purpose of a sanction is to punish. It is not uncommon for the beneficiary of that punishment to be the opposing party who thereby receives a windfall.").

Given the broad language utilized and the clear intent to strengthen these sanctions to allow for additional deterrence, there is no basis to conclude that there was any intent to limit "other appropriate relief" to compensatory sanctions such as "reasonable expenses and attorney's fees," and to exclude non-compensatory punitive sanctions. For the same reason that the evidence exclusion sanction was insufficient to foster deterrence, such a restriction on the "other appropriate relief" would frustrate the provision's deterrent purpose especially because, as the bankruptcy court also emphasized, "[t]here are also many instances in which awarding attorney's fees and costs may prove insufficient 'to deter those who might be tempted to such conduct in the absence of such a deterrent.'" *Gravel II*, 601 B.R. at 886 (quoting *Roadway Express, Inc. v. Piper*, 447 U.S. 752, 764 (1980)).

In addition to the shared purpose of deterrence, the scope of the intended sanctions under Rule 3002.1 cannot be distinguished from those under Rule 37 based upon the other interests that each rule is designed to protect. Thus, I respectfully disagree with the majority's view that Rule 3002.1 only protects the debtor in "remedying or avoiding certain costs," while Federal Rule 37 "protects the interests of the parties, the court, and the public in a speedy and just resolution of the case." Maj. Op. at 27. To be sure, as noted above, Rule 3002.1 seeks to ensure

that the debtor avoids certain undisclosed costs. However, more fundamentally, its objective is to broadly protect Chapter 13 debtors' opportunity for a "fresh start," which is one of the "twin pillars of the bankruptcy system." *In re Sanchez*, 372 B.R. 289, 321 (Bankr. S.D. Tex. 2007); *see also In re Rivera*, 599 B.R. 335, 342 (Bankr. D. Ariz. 2019) ("[Rule 3002.1] is a procedural mechanism designed to effectuate the Chapter 13 policy of providing debtors with a fresh start." (internal quotation marks omitted)). The reimbursement of costs to a debtor for a Rule violation (where such costs are incurred) does little to prevent future violations and therefore falls far short of safeguarding the Chapter 13 "fresh start" process for all such debtors. *See generally In re Lescinskas*, 628 B.R. at 384 ("Contrary to the bank's suggestion, putting a debtor in the difficult position of having to seek to amend his plan to amortize post-petition fees and charges (something a debtor cannot even force a lender to accept) is not an acceptable alternative to the lender's complying with Rule 3002.1(c) in the first instance.").

One of the primary reasons that the award of costs and attorney's fees may provide woefully insufficient deterrence is that debtors may often pay the fees and charges that violate the Rule, either because they go unnoticed to the debtor or because it is easier to pay the small fees/charges rather than to litigate them, and

such decisions by the debtor expose the offending party to no sanction whatsoever. The *amicus* brief from the National Association of Chapter 13 Trustees explained this economic incentive for non-compliance with the Rule by mortgage servicers:

> [PHH] waves off its errors, in part, by emphasizing the relatively small dollar amount at issue in these cases. But that misses the systemic point. These types of undisclosed fees are at the heart of the problem that Rule 3002.1 attempts to address. When fees and charges creep into accounts without proper notice, debtors may pay them, even if invalid. That may be because the fees and charges are not designated as immediately collectible and simply inflate the amounts debtors must pay to satisfy the loans. Or it may be because debtors conclude that the burden of challenging the amounts exceeds the likely benefit – especially if they learn of the exaggerated payoff only when they are attempting to close a refinancing of the loan or a sale of the mortgaged property. If the only cost to a claimholder for improperly assessing fees is to occasionally forego the (relatively small) fees when caught, it encourages servicers to just treat those forfeitures as a cost of doing business and never take the systemic measures required to service loans properly in Chapter 13.

Nat'l Assoc. of Chapter 13 Trs. Amicus Br. at 5–6 (citation omitted); *see also id*. at 15 ("[A]s bad as the headline-grabbing cases are, the real story is in the systemic errors that impose relatively small costs on a wide range of consumers. These errors are at least as pernicious because of the ease with which they can escape notice and because of the practical obstacles to obtaining individual relief."). The majority nevertheless asserts that, when the improper fees are contained on the monthly statements but not part of the amount due and ultimately did not get paid

(as is the case here), "[t]he rest is hyperventilation." Maj. Op. at 31. I do not view these serious concerns about systemic non-compliance by some mortgage servicers with the Rule and the Rule's inability to adequately address serial violations through compensatory sanctions, which were articulated by the *amicus* and recognized by a bankruptcy court with real-world expertise in the enforcement of this Rule, as "hyperventilation."

In short, beyond any interest that a particular debtor may have in the enforcement of the Rule, the bankruptcy courts and the public have an equally important and independent interest in ensuring that the "fresh start" objective of Chapter 13 proceedings is not undermined, and that a speedy and just resolution of those proceedings takes place. *See In re Sutherland*, 161 B.R. 657, 661 (Bankr. E.D. Ark. 1993) ("The longer the process to confirmation [under Chapter 13], the greater the harm to the creditors and the increase in adequate protection issues and problems for the creditors, the debtor, and the Court."); *see also In re Carr*, 468 B.R. 806, 808 (Bankr. E.D. Va. 2012) ("The purpose of Rule 3002.1 was to provide a prompt, efficient, and cost-effective means to determine whether there is a question as to the status of a debtor's home loan at the conclusion of the [C]hapter

13 case."); *Lucoski v. I.R.S.*, 126 B.R. 332, 342 (S.D. Ind. 1991) (noting that "speedy resolution of Chapter 13 proceedings are favored").

Thus, the judicial branch and the public have a compelling interest in ensuring that the bankruptcy process is not abused by Rule violations or other misconduct. In fact, it is the role of the Trustee to represent the public interest with regard to the enforcement of the bankruptcy rules, including Rule 3002.1. *See generally In re Zarnel*, 619 F.3d 156, 162 (2d Cir. 2010) (quoting other cases for the proposition that "the U.S. trustees are responsible for protecting the public interest and ensuring that bankruptcy cases are conducted according to law" and "avoiding substantial abuse of the bankruptcy process" (internal quotation marks omitted)).

In sum, I conclude that the plain meaning of "other appropriate relief" under Rule 3002.1, as confirmed by its modeling after both Rule 37 and that Rule's purpose, authorizes a bankruptcy court to use its discretion to impose punitive monetary sanctions in appropriate circumstances for violations of Rule 3002.1.

C. Sanctions Under a Bankruptcy Court's Inherent Power

Even assuming, *arguendo*, that the bankruptcy court did not have the authority to impose punitive monetary sanctions against PHH under Rule 3002.1,

the bankruptcy court certainly possessed the authority and discretion to impose the $75,000 in sanctions for PHH's Rule violations under its inherent powers.

As the majority correctly explains, it is well settled that "'[b]ankruptcy courts, like Article III courts, possess inherent sanctioning powers,' which 'include[s] the power to impose relatively minor non-compensatory sanctions on attorneys appearing before the court in appropriate circumstances.'" Maj. Op. at 28 (second alteration in original) (quoting *In re Sanchez*, 941 F.3d 625, 628 (2d Cir. 2019)). That inherent power can be exercised to address violations of rules, even where rules contain a sanctions provision. *See Chambers v. NASCO, Inc.*, 501 U.S. 32, 50 (1991) (explaining that if "neither the statute nor the Rules are up to the task, the court may safely rely on its inherent power"); *see also DLC Mgmt. Corp. v. Town of Hyde Park*, 163 F.3d 124, 136 (2d Cir. 1998) ("[T]he fact that there may be a statute or rule which provides a mechanism for imposing sanctions of a particular variety for a specific type of abuse does not limit a court's inherent power to fashion sanctions, even in situations similar or identical to those contemplated by the statute or rule.").

Notwithstanding its recognition of this inherent power possessed by the bankruptcy court, the majority concludes that the bankruptcy court here only

"alluded to its inherent powers" and that "[t]he sanction was imposed under Rule 3002.1(i)." Maj. Op. at 28–29. To be sure, an award of sanctions "may be exercised only on the basis of the specific authority invoked by that court." *In re Kalikow*, 602 F.3d 82, 96 (2d Cir. 2010). However, the bankruptcy court did more than "allude[] to its inherent powers" – it explicitly invoked such powers. More specifically, in both its opinion and its separate order, the bankruptcy court stated that it "finds, first, it has the authority pursuant to Rule 3002.1, pertinent caselaw, and *its inherent powers*, to impose punitive sanctions on PHH for its violations of Rule 3002.1." *Gravel II*, 601 B.R. at 878 (emphasis added); *see also id.* at 912. Thus, it is abundantly clear from the record that the bankruptcy court's inherent powers were invoked and that the sanctions were imposed pursuant to such powers (in addition to under the Rule). In fact, counsel for PHH even corrected the Court at oral argument to make clear that the bankruptcy court imposed the sanctions under its Rule 3002.1 and its inherent powers in its second order. *See* Oral Arg. at 8:15–28.

I also respectfully disagree with the majority's conclusion that the bankruptcy court did not sufficiently assess whether the sanction was authorized so as to allow this Court to reach the question. Although the bankruptcy court did

not include a section in the opinion separately discussing its basis for invoking its inherent authority to impose the $75,000 in sanctions for PHH's violations of Rule 3002.1, no such separate analysis was necessary because its factual basis for invoking its inherent powers was exactly the same as its basis for imposing such sanctions under Rule 3002.1, as to which there already was a lengthy and thorough analysis.

Moreover, the bankruptcy court spent several pages of its decision analyzing multiple inherent powers cases in great detail in discussing and determining the potential amount of the sanctions to be imposed under the court's inherent powers. *See Gravel II*, 601 B.R. at 905–07. Thus, this is not a case where the bankruptcy court failed to show "care, specificity, and attention to the sources of its power," *In re Kalikow*, 602 F.3d at 96 (quoting *Sakon v. Andreo*, 119 F.3d 109, 113 (2d Cir. 1997)); *cf. Sakon*, 119 F.3d at 113 ("[A]n award [of sanctions] either without reference to any statute, rule, decision, or other authority, or with reference only to a source that is inapplicable will rarely be upheld.").

Indeed, it is hard to imagine (and the majority fails to articulate) what additional factual or legal reasoning would be needed to aid our review of this determination under the bankruptcy court's inherent powers. Interestingly, PHH

has not even argued that the bankruptcy court's reasoning with respect to its inherent powers was deficient. Instead, when asked at oral argument about the imposition of the $75,000 in sanctions under its inherent authority, PHH's counsel simply stated, "with respect to the $75,000 part of the case, . . . [the Trustee] has a stronger argument there." Oral Arg. at 5:17–33. In short, I conclude that the bankruptcy court's decision – including its explicit invocation of its inherent powers, its detailed findings with respect to PHH's violations of Rule 3002.1, and its thorough explanation as to how it arrived at the particular amount of the sanctions under the applicable case authority for making such a determination under its inherent powers – provided a more than sufficient record for this Court to analyze and conclude that the bankruptcy court did not abuse its discretion in imposing such sanctions.

As to the requirements for the exercise of that authority and discretion under a bankruptcy court's inherent powers, although the majority suggests that it is "dubious" that a bankruptcy court can impose monetary sanctions without an explicit finding of bad faith, the Supreme Court has made clear that monetary sanctions imposed under a court's inherent powers require a finding that the misconduct "constituted or was *tantamount to bad faith*." *Roadway Express, Inc.*, 447

U.S. at 767 (emphasis added). As to the nature of conduct that can be "tantamount to bad faith," we have explained that "a federal court – any federal court – may exercise its inherent power to sanction a party . . . who has acted in bad faith, *vexatiously, wantonly, or for oppressive reasons*." *Ransmeier v. Mariani*, 718 F.3d 64, 68 (2d Cir. 2013) (emphasis added) (internal quotation marks omitted).

Therefore, although courts often make an explicit finding of bad faith on behalf of a party before imposing sanctions, *see Int'l Techs. Mktg., Inc. v. Verint Sys., Ltd.*, 991 F.3d 361, 368 (2d Cir. 2021), a court may impose a monetary sanction on a party (or an attorney) under its inherent power if the factual findings supporting the sanctions are tantamount to bad faith, *see, e.g.*, *First Bank of Marietta v. Hartford Underwriters Ins. Co.*, 307 F.3d 501, 520–21 (6th Cir. 2002) (concluding that, although the district court's finding that the plaintiff's conduct was "laced with bad faith" was an explicit finding of bad faith, "the district court's other findings [that] Plaintiff's litigation conduct [was] 'tantamount' to bad faith provid[ed] more than ample grounds to justify the exercise of its inherent authority and to impose the sanction of attorney fees and costs").

Here, the bankruptcy court observed, in its initial opinion imposing the sanctions, that:

> [w]hile there is no requirement to make a bad faith finding, *PHH's conduct cannot realistically be attributed to an innocent mistake*. PHH *had knowledge* of [its obligations] . . . , only corrected the statements after the Trustee filed a motion for sanctions, and then asserted it did not violate a court order at all. Taken together, particularly in the context of prior court warnings, these actions raise serious concerns about *whether PHH is making a good faith effort to comply with Rule 3002.1* and heed the directives of court orders declaring debtors current.

In re Gravel ("*Gravel I*"), 556 B.R. 561, 576 n.10 (Bankr. D. Vt. 2016) (emphases added), *vacated and remanded by PHH Mortg. Corp. v. Sensenich*, Case No. 5:16–cv–00256–gwc, 2017 WL 6999820 (D. Vt. Dec. 18, 2017). In addition to this finding in the initial opinion that PHH's conduct was not "an innocent mistake," the bankruptcy court reiterated in its second opinion (re-imposing the sanctions) that it had found that "PHH had engaged in a pattern of the offending conduct" and "PHH had previously been admonished twice and sanctioned once (in this Court) for sending incorrect statements." *Gravel II*, 601 B.R. at 882; *see also id.* at 896, 903 (emphasizing "PHH's status as a repeat offender" and "the gravity of [PHH's] misconduct").

Simply put, the record is replete with findings by the bankruptcy court of PHH's repeated violations of the Rule despite having the wherewithal to know better and its assurances to the bankruptcy court that it would amend its processes

to comply with its obligations. In my view, that record is more than sufficient to constitute the finding, which was necessary to support monetary sanctions under the bankruptcy court's inherent powers, that PHH's conduct was "tantamount to bad faith." *Roadway Express, Inc.*, 447 U.S. at 767; *see also Matter of Betts*, Nos. 94–2018, 94–2668, 1995 WL 108940, at *2 (7th Cir. 1995) (imposing sanction on an attorney pursuant to a bankruptcy court's inherent powers based on "egregious misconduct"); *In re AOV Indus., Inc.*, 798 F.2d 491, 498 (D.C. Cir. 1986) (noting the litigant "was on clear notice of what action was expected of him in the district court: the Bankruptcy Rules, the district judge, and the motion for fees made it crystal clear" what action the litigant must take, and sanctions were appropriate because he did not do so).

In any event, even if the bankruptcy court's reasoning for the imposition of sanctions under its inherent powers (including on the issue of bad faith) was not sufficiently developed to allow review by this Court (as the majority finds), we should remand the matter, and the bankruptcy court should be afforded the opportunity to provide additional reasoning for its determination. *See, e.g.*, *Hollon v. Merck & Co.*, 589 F. App'x 570, 572 (2d Cir. 2014) (remanding where the district court did not provide sufficient reasoning to allow appellate review on the issue

of bad faith for the imposition of sanctions under the court's inherent powers); *Weaver v. Chrysler Corp.*, 14 F. App'x 136, 137 (2d Cir. 2001) (holding that findings for imposition of sanctions were insufficient and "retain[ing] jurisdiction over th[e] appeal while vacating the order and remanding to the district court for additional findings and reasoning as appropriate"), *order rescinded*, 99 F. App'x 330, 333 (2d Cir. 2004) (affirming district court's imposition of sanctions after it issued a supplemental order "in light of [its] additional findings and articulated reasoning"). Here, the bankruptcy court is not being afforded such an opportunity to supplement the record on remand.

In short, I conclude that the record is sufficient to allow this Court to determine that the bankruptcy court did not abuse its discretion in imposing sanctions under its inherent powers for PHH's flagrant misconduct in repeatedly violating Rule 3002.1 even after prior sanctions, warnings from bankruptcy courts, and a representation by PHH that it would rectify any internal controls that were contributing to such violations.

D. The Amount of the Sanctions

Although the majority did not need to analyze the amount of the sanctions in light of its holdings, I briefly write to explain why there would have been no

basis to disturb the bankruptcy court's determination that $75,000 was the appropriate amount.

As a threshold matter, given that PHH is a multi-billion- dollar company, $75,000 was a modest, non-serious sanction that did not present the type of financial impact on PHH that would warrant heightened due process requirements. *See, e.g.*, *United States v. Twentieth Century Fox Film Corp.*, 882 F.2d 656, 665 (2d Cir. 1989) ("We conclude that the jury right is available for a criminal contempt whenever the fine imposed on an organization exceeds $100,000. For fines below the $100,000 threshold, it will remain appropriate to consider whether the fine has such a significant financial impact upon a particular organization as to indicate that the punishment is for a serious offense, requiring a jury trial."); *CBS Broad. Inc. v. FilmOn.com, Inc.*, 814 F.3d 91, 103–04 (2d Cir. 2016) (finding that a $90,000 sanction against an internet company was "relatively minor"); *cf. Mackler Prods., Inc. v. Cohen*, 146 F.3d 126, 130 (2d Cir. 1998) (concluding "the imposition of a $10,000 punitive sanction on an individual (*as opposed to a corporation or collective entity*) requires" certain heightened due process protections (emphasis added)); *see also Sizzler Family Steak Houses v. Western Sizzlin Steak House, Inc.*, 793 F.2d 1529,

1535 (11th Cir. 1986) (characterizing a $25,000 contempt sanction imposed against corporate restaurant chain as "a modest sanction").

With respect to the determination as to the amount of the sanction, the bankruptcy court properly considered the amount that would be necessary to provide deterrence in light of PHH's ability to pay and its sophistication. *See Oliveri v. Thompson*, 803 F.2d 1265, 1281 (2d Cir. 1986) ("[I]t lies well within the district court's discretion to temper the amount to be awarded against an offending [person or entity] by a balancing consideration of his [or its] ability to pay."); *see also Farmer v. Banco Popular of N. Am.*, 791 F.3d 1246, 1259 (10th Cir. 2015) ("[B]ecause the principal purpose of punitive sanctions is deterrence, the offender's ability to pay must be considered."); *Johansen v. Combustion Eng'g, Inc.*, 170 F.3d 1320, 1338 (11th Cir. 1999) ("A bigger award is needed to attract the attention of a large corporation." (alteration and internal quotation marks omitted)). In particular, in its initial opinion, the bankruptcy court explained:

> [T]he Court must take into account that PHH is a sophisticated commercial lender and an entity of substantial financial means. According to the public statements on its website, PHH is a top-ten originator and servicer of residential mortgages in the United States, boasting approximately $41 billion in mortgage financing and maintained an average servicing portfolio of approximately 1.1 million loans in 2015 alone. PHH has the expertise and experience to be charged with knowledge of the Bankruptcy Rules, of its duty to

> comply with court orders, and of its obligation to fulfill the commitments it makes to courts and debtors.

Gravel I, 556 B.R. at 578 (footnote and internal quotation marks omitted). The bankruptcy court also addressed that factor in its second opinion. *See, e.g.*, *Gravel II*, 601 B.R. at 901 ("PHH administers millions of dollars in mortgages every day, and therefore it is all too easy for it to pay a $10,000 sanction as a cost of doing business, and there is no way of selecting a specific amount that will *necessarily deter*." (internal quotation marks omitted)).

Similarly, it was well within the bankruptcy court's discretion to link the amount of the sanctions to the number of violations. *See Int'l Techs. Mktg.*, 991 F.3d at 369 (holding that the "number of misrepresentations that a party makes are perfectly acceptable data points for a court to consider in determining whether – and, perhaps more importantly, *what* – sanctions are warranted"). Here, the bankruptcy court determined that a sanction of $1,000 per violation should be imposed in light of PHH's repeated violations. Because PHH violated Rule 3002.1 on twenty-five separate occasions in each of the three cases, the bankruptcy court's formula resulted in a total of $75,000 in sanctions. That determination, especially in light of the prior sanction against PHH for the same misconduct and its sophistication, was not an abuse of discretion.

* * *

In sum, I conclude that the bankruptcy court did not exceed its authority or abuse its discretion in imposing $75,000 in sanctions against PHH under either Rule 3002.1 or its inherent powers for the reasons set forth above, and therefore, I respectfully dissent from the portion of the majority's opinion which vacated the imposition of those sanctions.

20-1-bk (L)
In re: Gravel

United States Court of Appeals for the Second Circuit

AUGUST TERM 2020
Nos. 20-1-bk(L), 20-2-bk, 20-3-bk

IN RE: NICHOLAS GRAVEL, AMANDA GRAVEL,
Debtors.

PHH MORTGAGE CORPORATION,
Creditor-Appellant,

v.

JAN M. SENSENICH,
Trustee-Appellee.

ARGUED: FEBRUARY 4, 2021
DECIDED: AUGUST 2, 2021

Before: JACOBS, BIANCO, PARK, Circuit Judges.

PHH Mortgage Corp. appeals from the order of the United States Bankruptcy Court for the District of Vermont (Brown, J.) imposing sanctions in three chapter 13 cases. PHH was sanctioned $75,000 for violation of Bankruptcy Rule of Procedure 3002.1 and $225,000 for violation of bankruptcy court orders.

PHH argues that Rule 3002.1 does not authorize punitive monetary sanctions, and that PHH did not violate the court orders as a matter of law. We agree.

We VACATE the sanctions order and REVERSE.

JUDGE BIANCO concurs in part and dissents in part in a separate opinion.

MATTHEW J. DELUDE, Primmer Piper Eggleston & Cramer PC, Manchester, NH (Alexandra E. Edelman, Douglas J. Wolinsky, on the brief) for Creditor-Appellant PHH Mortgage Corp.

MAHESHA P. SUBBARAMAN, Subbaraman PLLC, Minneapolis, MN, for Trustee-Appellee Jan M. Sensenich.

Henry E. Hildbrand, III, Nashville, TN, for Amicus Curiae National Association of Chapter 13 Trustees.

Tara Twomey, National Consumer Bankruptcy Rights Center, San Jose, CA, for Amici Curiae National Consumer Bankruptcy Rights Center, National Association of Consumer Bankruptcy Attorneys, National Consumer Law Center, Legal Services Vermont, Inc., and Housing Clinic of Jerome N. Frank Legal Services Organization at Yale Law School.

DENNIS JACOBS, Circuit Judge:

This appeal involves punitive sanctions imposed in three chapter 13 cases in Vermont. The debtor households are the Gravels, the Beaulieus, and the Knisleys. The sanctioned party is the creditor-appellant PHH Mortgage Corp., which holds or services the mortgage on the principal residence of each debtor household. The appellee, Jan Sensenich, is the chapter 13 standing Trustee for the District of Vermont. The Trustee shepherds the debtors through the chapter 13 process and oversees their payments to PHH under their respective chapter 13 plans.

PHH sent monthly mortgage statements listing fees totaling $716 that had not been properly disclosed in the three cases. The United States Bankruptcy Court for the District of Vermont (Brown, J.) sanctioned PHH $225,000 for violation of court orders issued in the Gravel and Beaulieu cases, which declared that the debtors were current on their mortgages and enjoined PHH from challenging that fact in any other proceeding.

The bankruptcy court also sanctioned PHH $75,000 for violation of Bankruptcy Rule of Procedure 3002.1 in all three cases. Rule 3002.1(c) requires

that a creditor give formal notice to the debtor and trustee of new post-petition fees and charges, and it gives the bankruptcy court power to impose sanctions for non-compliance.

The bankruptcy court's sanctions order was certified for direct appeal. We hold that Rule 3002.1 does not authorize punitive monetary sanctions, and that PHH did not, as a matter of law, violate the court orders.

The sanctions order is VACATED and REVERSED.

BACKGROUND

Frustration with PHH began early in the Gravel case, which was filed in February 2011. The Gravels' plan provided for them to remain in their home while making "conduit" monthly mortgage payments for 60 months. Under the District of Vermont's bankruptcy procedures, the Gravels paid the Trustee who then disbursed the payment to PHH.

Pursuant to a (since superseded) standing order, the Trustee accounted for the payments in March and April as an "administrative arrearage" rather than as a regular post-petition monthly mortgage payment. In effect, those payments

were treated as a pre-petition arrearage paid as a special claim, so that regular post-petition payments did not begin until the third month. Monthly payments were thus forwarded to PHH as regular mortgage payments beginning with May. Because of this accounting, PHH incorrectly termed the loan delinquent and began to add late penalties on mortgage payments for March and April. PHH sent monthly mortgage statements reflecting this delinquency, and the Trustee responded with three letters in 2012 and 2013 explaining PHH's error, to which PHH failed to respond.

When PHH threatened foreclosure, the Trustee in February 2014 moved to compel PHH to apply the mortgage payments as provided by the chapter 13 plan. The Trustee also requested an award of sanctions to the debtors. PHH corrected the mortgage statements to reflect that the Gravels were current on post-petition payment obligations. PHH promised to prevent future errors. The parties stipulated to a $9,000 sanction, which the bankruptcy court so-ordered in March 2014. (The $9,000 sanction is not the subject of this appeal.)

* * *

Two years later, the Gravels reached the end of their chapter 13 plan. An order on May 20, 2016, confirmed that the Gravels were "current." J. App'x 705. That is, the Gravels had cured all pre-petition arrearages or defaults existing when the case was filed, and made all post-petition payments. (An identical order was issued in the Beaulieu case; they are referenced as "Current Orders.")

When PHH sent another monthly mortgage statement five days later, the Trustee noticed that an old charge for "property inspection fees" was listed under the "loan information" section. Id. at 654. The statement specified that the recorded fee and other account information was provided to comply with local bankruptcy rules and was "not an attempt to collect a debt." Id. Further, the fee--which had grown to $258.75 over at least 25 monthly statements--was not reflected in the "total payment due." Id. The only payment due was the principal/interest and escrow.

Nevertheless, the Trustee moved for a finding of contempt and sanctions on the ground that the charge violated the Current Order, and that each of the 25 charges violated Bankruptcy Rule 3002.1. Rule 3002.1 governs installment

payments on a home mortgage in a plan under chapter 13. Fed. R. Bankr. P. 3002.1(a). Under the rule, a mortgage creditor "shall file and serve on . . . the trustee a notice itemizing all fees, expenses, or charges" that the creditor "asserts are recoverable against the debtor" and serve this notice "within 180 days after the date on which the fees, expenses, or charges are incurred." Fed. R. Bankr. P. 3002.1(c). If a creditor fails to comply, a bankruptcy court may preclude the creditor from presenting the claim as evidence in the case, or award the debtor other relief including expenses and attorney's fees. Fed. R. Bankr. P. 3002.1(i).

In response to the Trustee's motion, PHH admitted that the fee had not been properly noticed within 180 days under Rule 3002.1, removed the fee from the Gravels' mortgage statement, and opposed the motion for sanctions.

* * *

Late-noticed fees also appeared on the Beaulieus' monthly mortgage statements. They filed their chapter 13 case in March 2011. The statements began reflecting a fee for insufficient funds 18 months later and a charge for property inspection two years later; and those fees were still being listed when the bankruptcy court issued the Current Order on May 5, 2016. Twenty days

later, PHH sent the Beaulieus a monthly statement, on which the fees were still listed. The insufficient funds fee was $30, and the property inspection fee was $56.25.

Around the time the Trustee filed its motion in the Gravel case, the Trustee moved for a finding of contempt and sanctions in the Beaulieu case on the same basis. PHH removed the charges from the Beaulieus' mortgage statement and opposed the motion.

* * *

Post-filing of the Knisley case, 25 monthly mortgage statements showed a late charge and property inspection fee that had not been properly disclosed within 180 days. The late charge was $124.50, and the property inspection was $246.50. The Trustee moved for sanctions under Rule 3002.1(i), and PHH removed the charge and fee and opposed the motion. PHH was not alleged to be in contempt of a current order because no current order had issued; the Knisleys had not reached the end of their plan.

* * *

After a consolidated hearing, the bankruptcy court granted the Trustee's motions in September 2016. It found that PHH had violated Rule 3002.1(c) 25 times in each case, as well as the two Current Orders. It sanctioned PHH $75,000 pursuant to Rule 3002.1(i). And it sanctioned PHH for the Current Orders violation pursuant to its inherent power and § 105 of the Bankruptcy Code: $200,000 in the Gravel case and $100,000 in the Beaulieu case.

The bankruptcy court noted that it "levies this substantial penalty on PHH to convey a clear message to PHH, and other mortgage creditors, that they may not violate court orders with impunity and will suffer significant monetary sanctions if they conduct their mortgage accounting operations in a manner that fails to fully comply with Rule 3002.1, violates court orders, or threatens the fresh start of Chapter 13 debtors." In re Gravel ("Gravel I"), 556 B.R. 561, 580 (Bankr. D. Vt. 2016), vacated and remanded sub nom. PHH Mortg. Corp. v. Sensenich, No. 5:16-CV-00256, 2017 WL 6999820 (D. Vt. Dec. 18, 2017). PHH was ordered to pay the $375,000 to "Legal Services Law Line of Vermont." Id.

The United States District Court for the District of Vermont (Crawford, J.) vacated both sanctions. It held that the $75,000 and $300,000 sanctions exceeded the bankruptcy court's "statutory and inherent powers" because it lacks power to impose "serious punitive sanctions." PHH Mortg. Corp., 2017 WL 6999820, at *7–8. The district court reasoned that bankruptcy courts are ill-equipped to provide the procedural protections that due process requires, and that bankruptcy judges lack the tenure and compensation protections that ensure the judicial independence of Article III judges. The district court observed that the sanctions here were far greater than a punitive sanction of $50,000 that the Ninth Circuit vacated for the same reasons in In re Dyer, 322 F.3d 1178, 1194 (9th Cir. 2003). Remanding the matter, the district court noted that the bankruptcy court may refer a matter for criminal contempt proceedings and sanctions, or may "take steps to enforce its orders short of punitive sanctions of the scope and type imposed in these cases." PHH Mortg. Corp., 2017 WL 6999820, at *9.

The bankruptcy court issued a second sanctions order (the one now before us). See In re Gravel ("Gravel II"), 601 B.R. 873, 903 (Bankr. D. Vt. 2019). It adopted the factual findings of the first order and imposed the same sanctions

for the Rule 3002.1 violation. However, the sanctions for violation of the Current Orders were reduced 25%: from $200,000 to $150,000 in the Gravel case and from $100,000 to $75,000 in the Beaulieu case. The reduced Current Orders sanctions were still to be paid to Legal Services; but the Trustee was made the recipient of the Rule 3002.1 sanction.

PHH appealed the second sanctions order to the district court, but the Trustee requested the bankruptcy court to certify the order for direct review by this Court, which the bankruptcy court granted. The Trustee petitioned this Court for direct review, which we granted.

DISCUSSION

A. Jurisdiction

This case is before us on direct appeal from the bankruptcy court's second sanctions order. Under 28 U.S.C. § 158(d)(2), a court of appeals has jurisdiction when the bankruptcy court has certified that an order involves an unresolved question of law and the court of appeals authorizes a direct appeal of that order.

There is no doubt that we have jurisdiction to review the second sanctions order; but we must first clarify the scope of our jurisdiction over this appeal.

The bankruptcy court certified three questions of law. The questions, which the Trustee formulated, concern the power of bankruptcy courts to impose "punitive non-contempt sanctions" under Rule 3002.1, to impose such sanctions under § 105(a), and to impose them "commensurate (in amount) to the violation at hand." In re Gravel, No. 11-10112, 2019 WL 3783317, at *2 (Bankr. D. Vt. Aug. 12, 2019). We authorized direct review.

The Trustee contends that we can (or should) answer all three questions because they were certified. The statute, however, authorizes appeals of "orders," not "questions," and the second sanctions order is the only order on review. See 28 U.S.C. § 158(d)(2)(A). Unless that order poses a question of law, we lack jurisdiction to answer it notwithstanding what questions are certified. See N.Y.C. Health & Hosps. Corp. v. Blum, 678 F.2d 392, 396–97 (2d Cir. 1982) (observing the same with respect to 28 U.S.C. § 1292). Otherwise, we would be rendering an advisory opinion. See Preiser v. Newkirk, 422 U.S. 395, 401 (1975).

We may answer the certified questions only insofar as they help resolve the questions of law raised in the issues on appeal: whether the bankruptcy court properly sanctioned PHH for violating the Current Orders, and whether the bankruptcy court properly sanctioned PHH for violating Rule 3002.1.

B. Standard of Review

A bankruptcy court's award of sanctions, including findings of contempt, are reviewed for abuse of discretion. In re Kalikow, 602 F.3d 82, 91 (2d Cir. 2010). A bankruptcy court "necessarily abuses its discretion if it based its ruling on an erroneous view of the law or on a clearly erroneous assessment of the evidence." Id. (quoting In re Highgate Equities, Ltd., 279 F.3d 148, 152 (2d Cir. 2002)) (brackets omitted).

The bankruptcy court's factual determinations are reviewed for clear error. U.S. Polo Ass'n, Inc. v. PRL USA Holdings, Inc., 789 F.3d 29, 33 (2d Cir. 2015). Questions of law and interpretation of an order underlying a contempt finding are reviewed de novo. Id.

C. The $225,000 Sanction

PHH argues that the $225,000 sanction was an abuse of discretion because PHH did not, as a matter of law, violate the Current Orders. We agree. Though the orders declared that the debtors were current, they did not enjoin the recording of expired fees on the statements. Without an express injunction, there is fair ground of doubt as to whether the listed fees can form the basis for contempt.

A bankruptcy court's contempt power, like that of a district court, is "narrowly circumscribed." Perez v. Danbury Hosp., 347 F.3d 419, 423 (2d Cir. 2003); see Taggart v. Lorenzen, 139 S. Ct. 1795, 1801 (2019) ("[T]he bankruptcy statutes incorporate the traditional standards in equity practice for determining when a party may be held in civil contempt for violating an injunction."). Accordingly, "our review of a contempt order is more exacting than under the ordinary abuse-of-discretion standard." Perez, 347 F.3d at 423; see United States v. Local 1804-1, Int'l Longshoremen's Ass'n, 44 F.3d 1091, 1095 (2d Cir. 1995) ("The contempt power is different.").

Given the restricted scope of the contempt power, a prior question is whether the sanction here was actually based on contempt. The bankruptcy court invoked its "authority . . . to impose punitive sanctions on parties who violate court orders," observing that it "may hold a creditor in contempt for that party's violation of an injunction order." Gravel II, 601 B.R. at 903. Then, applying the Supreme Court's recently-articulated standard for contempt in Taggart, the bankruptcy court "impos[ed] punitive sanctions on PHH for its violation of the Debtor Current Orders." Id. at 903; see also id. at 888–89. Moreover, the Trustee's motion was one "for contempt and sanctions." J. App'x 651. The bankruptcy court plainly based its sanction on contempt.

The Trustee argues that we should affirm because a bankruptcy court, in any event, has power to issue "non-contempt-based sanctions." Appellee's Br. at 41. This argument is misplaced. A bankruptcy court's "discretion to award sanctions may be exercised only on the basis of the specific authority invoked by that court." Kalikow, 602 F.3d at 96. We therefore "confine our review to the question of whether the court properly exercised that power" and "do not consider potential alternative sources of authority." In re Sanchez, 941 F.3d 625,

626–27 (2d Cir. 2019). Because the bankruptcy court here relied on its contempt power, our review is limited to whether it abused its discretion in exercising that power.

* * *

A bankruptcy court's contempt power derives from a court injunction and 11 U.S.C. § 105(a). An injunction is an equitable remedy, and § 105(a) authorizes issuance of any "order" that is "necessary or appropriate to carry out the provisions of [the Bankruptcy Code]." Together, they "bring with them the 'old soil' that has long governed how courts enforce injunctions." Taggart, 139 S. Ct. at 1801. That includes the "'potent weapon' of civil contempt." Id. (quoting Int'l Longshoremen's Ass'n, Local 1291 v. Phila. Marine Trade Ass'n, 389 U.S. 64, 76 (1967)).

Under Taggart, a bankruptcy court may hold a creditor in contempt for violating the court's injunction only "if there is *no fair ground of doubt* as to whether the order barred the creditor's conduct." Id. at 1799. The "fair ground of doubt" standard has long been used in this Circuit to determine when a party may be held in contempt in the district court. See King v. Allied Vision, Ltd., 65

F.3d 1051, 1058 (2d Cir. 1995) (quoting Cal. Artificial Stone Paving Co. v. Molitor, 113 U.S. 609, 618 (1885)). The standard derives from two principles that are reemphasized in Taggart: "civil contempt is a severe remedy" and "basic fairness requires that those enjoined receive explicit notice of what conduct is outlawed." 139 S. Ct. at 1802 (cleaned up). In particular, a contempt order is warranted only where the party has notice of the order, the order is clear and unambiguous, and the proof of noncompliance is clear and convincing. King, 65 F.3d at 1058; see U.S. Polo, 789 F.3d at 33.

The Current Orders had two components relevant to the contempt finding. The orders declared that the Gravels and Beaulieus are current on their mortgage payments to PHH, including all charges:

> the debtors, by their payments through the Office of the Chapter 13 Trustee, have made all payments due during the pendency of this case . . . including all monthly payments and any other charges or amounts due under their mortgage with PHH Mortgage Corporation.

The orders also prohibited PHH from contesting that fact in any other proceeding:

> the mortgagee [PHH] shall be precluded from disputing that the debtors are current (as set forth herein) in any other proceeding.

J. App'x 705–06, 709. These paragraphs, the bankruptcy court held, gave PHH "notice it was enjoined from seeking to collect any fees or expenses allegedly incurred during the period encompassed by each Order, if not specified in the Order." Gravel II, 601 B.R. at 890. We disagree.

The Current Orders were not a clear and unambiguous prohibition on PHH's sanctioned conduct. To form the basis for contempt, an order must leave "no doubt in the minds of those to whom it was addressed . . . precisely what acts are forbidden." Drywall Tapers & Pointers of Greater N.Y., Local 1974 v. Local 530 of Operative Plasterers & Cement Masons Int'l Ass'n, 889 F.2d 389, 395 (2d Cir. 1989).

The declaration that a debtor is current does not in itself clearly forbid any conduct. Standing alone, it is an inadequate basis for contempt. The very purpose of the civil contempt power is to induce compliance with a court's injunction. Taggart, 139 S. Ct. at 1801. Aside from enjoining acts in other proceedings, there is no injunction here (or similar command or equitable

remedy) to enforce--i.e., the orders fail to describe an "act or acts restrained or required." Fed. R. Civ. P. 65(d)(1)(C); Fed. R. Bankr. P. 7065; see Steffel v. Thompson, 415 U.S. 452, 471 (1974) ("[N]oncompliance with [a declaratory judgment] may be inappropriate, but is not contempt."). And to imply a restraint where none is stated would violate the principle that a party must have "explicit notice" of what is forbidden or required. Taggart, 139 S. Ct. at 1802.

The Current Orders imposed a single injunction: PHH may not dispute the current status of the debtors "in any other proceeding." J. App'x 706, 709. However broad "other proceeding" may be in this context, there is fair ground of doubt as to whether it would reach PHH's out-of-court conduct in these proceedings.

The Trustee argues that, unless PHH is held in contempt, mortgage creditors will be able to assess improper fees with impunity. These concerns are overwrought. The bankruptcy court could have crafted an order that would have forbidden the conduct troubling the Trustee. The orders in Taggart, for example, relieved the debtor "from all debts that arose before the date of the order for relief" *and* operated "'as an injunction against the commencement or

continuation of an action, the employment of process, or an act, to collect, recover or offset' a discharged debt." 139 S. Ct. at 1799, 1801 (quoting 11 U.S.C. §§ 727, 524(a)(2)).

Although a bankruptcy court has "unique expertise in interpreting its own injunctions and determining when they have been violated," In re Anderson, 884 F.3d 382, 390–91 (2d Cir. 2018), this insight does not command deference. Anderson--in recognizing the expertise-- holds that a bankruptcy court is not required to compel arbitration of claims alleging violation of its discharge injunction. Id.; see also MBNA Am. Bank, N.A. v. Hill, 436 F.3d 104, 110 (2d Cir. 2006). But this Court still has a duty to conduct its own "exacting" review of contempt orders. Perez, 347 F.3d at 423. Expertise does not excuse a bankruptcy court from the fundamental limit on its power; a bankruptcy court cannot hold a party in contempt for violating an order that is subject to varying interpretations.

Moreover, the questionable proof of PHH's non-compliance could provide a second ground for vacatur, though we need not rely on it.[1] Because

[1] The mortgage statements excluded the fees at issue from the total payment due. The following, for example, is from the Beaulieus' statement:

"ambiguities and omissions in orders redound to the benefit of the person charged with contempt," Gucci Am., Inc. v. Weixing Li, 768 F.3d 122, 143 (2d Cir.

Dear Mr. and/or Ms.

Below is the monthly Bankruptcy statement for the above loan. This statement is provided with the intent of complying with the United States Bankruptcy Court Vermont District Permanent Rule (3071-1). *This is not an attempt to collect a debt.*

Loan Information:

Unpaid Principal balance:	$	11,851.98
Escrow Balance:	$	3,962.45
Maturity Date:		07-18
Interest Rate:		5.37500%
Contractual Due Date:		03-01-16
Post-Petition due date:		03-01-16
Late Charge Balance to date:	$	.00
NSF fees:	*$*	*30.00*
Property Inspection fees:	*$*	*56.25*
Interest Paid Year to Date:	$	485.79
Property Taxes Paid Year to Date:	$	.00

Breakdown of Contractual Monthly Payment:

Principal and Interest:	$	437.66
Escrow:	$	306.74
Total Payment Due:	*$*	*744.40*

J. App'x 675 (emphasis added).

2014), the Current Orders already lack the requisite clarity to hold PHH in contempt.

D. The $75,000 Sanction

The bankruptcy court imposed sanctions on PHH for violation of Bankruptcy Rule 3002.1 amounting to $25,000 in each case for the improperly-noticed fees listed on the mortgage statements. The sanction was calibrated to "the number of incorrect statements PHH sent" as opposed "to the amount of the charges on each incorrect statement," which in total across the three cases did not exceed $716 (and in fact were not even "charges" in any sense: they were not reflected in the balance due). Gravel II, 601 B.R. at 903. Thus, the bankruptcy court imposed a punitive sanction on PHH of $1,000 per statement to deter PHH from further non-compliance.

To impose the sanction, the bankruptcy court invoked Rule 3002.1's authorization to "award other appropriate relief" for violation of the rule. PHH argues that the bankruptcy court erred because "other appropriate relief" does not authorize punitive sanctions.

This is an issue of first impression among the circuit courts. And few bankruptcy courts have opined on it. Although one court declined to dismiss a plaintiff's claim for Rule 3002.1 sanctions in an adversary proceeding, In re Bivens, 625 B.R. 843, 850–51 (Bankr. M.D.N.C. 2021), it did not address the issue here. The bankruptcy court in this case is apparently the first and only one to impose punitive monetary sanctions under the rule. The only other court to have weighed in reached the opposite conclusion: that Rule 3002.1 "does not permit [the court] to impose punitive monetary sanctions." In re Tollstrup, No. 15-33924, 2018 WL 1384378, at *5 (Bankr. D. Or. Mar. 16, 2018); see also In re Reynolds, 470 B.R. 138, 144 (Bankr. D. Colo. 2012) (reaching similar conclusion that Rule 3001(c) does not authorize claim disallowance as a sanction). We agree.

* * *

Before Rule 3002.1 was adopted in 2011, mortgage holders would forbear asserting new obligations in the bankruptcy proceedings for fear of violating the automatic stay. The result was that debtors who had completed their chapter 13 plans were discovering that they had incurred new obligations and defaults. See

9 Collier on Bankruptcy ¶ 3002.1.RH (16th 2020); Fed. R. Bank. P. 3002.1 Advisory Committee Notes to 2011 Adoption.

As a solution, Rule 3002.1 ensures that debtors are informed of new post-petition obligations (such as fees). The rule requires formal notice to debtors and trustees, and it assures creditors that they will not violate the automatic stay. Debtors then have a chance to pay or contest the new obligations, which prevents lingering deficits from surfacing after the case ends.

The last subdivision of the rule provides an enforcement mechanism. If a creditor fails to give the requisite notice, the bankruptcy court may preclude the creditor from presenting evidence of its claim in the case--unless the failure was substantially justified or harmless. Fed. R. Bankr. P. 3002.1(i)(1). The court may also (or instead) "award other appropriate relief, including reasonable expenses and attorney's fees caused by the failure." Fed. R. Bankr. P. 3002.1(i)(2).

Because "other appropriate relief" is a general phrase amid specific examples, it is best "construed in a fashion that limits the general language to the same class of matters as the things illustrated." Canada Life Assurance Co. v. Converium Ruckversicherung (Deutschland) AG, 335 F.3d 52, 58 (2d Cir. 2003).

Reasonable expenses and attorney's fees are compensatory forms of relief. They expressly remedy harms to the debtor "caused by the [creditor's] failure" to give proper notice of a claim. Fed. R. Bankr. P. 3002.1(i)(2). This suggests that "other appropriate relief" is limited to non-punitive sanctions, as that would cabin it to the most general attribute shared with an award of expenses and fees.

The rule's only other sanction reinforces that inference. It prevents a creditor from collecting an un-noticed claim so that a surprise deficiency does not later frustrate the debtor's fresh start. The rule makes an exception for harmless non-compliance, demonstrating that this evidence-preclusion sanction is tied to prejudice that a failure to notice causes the debtor. The sanction thus prospectively serves the remedial goal of shielding the debtor from unforeseen charges, and thus is also not a punishment.

Moreover, other sections of the Bankruptcy Code explicitly authorize punitive damages, whereas Rule 3002.1 is silent. See, e.g., 11 U.S.C. § 362(k)(1) ("[A]n individual injured by any willful violation of a stay provided by this section shall recover actual damages, including costs and attorneys' fees, and, in appropriate circumstances, may recover punitive damages.").

A broad authorization of punitive sanctions is a poor fit with Rule 3002.1's tailored enforcement mechanism and limited purpose. Punitive sanctions do not fall within the "appropriate relief" authorized by Rule 3002.1.

The bankruptcy court reasoned that Rule 3002.1 authorizes punitive sanctions because merely precluding evidence and awarding attorneys' fees might insufficiently deter misconduct, drawing an analogy to discovery sanctions under Federal Rule of Civil Procedure 37. The dissent likewise argues that Federal Rule 37 and Bankruptcy Rule 3002.1 have an "identical purpose." Dissent at 17. The analogy is unpersuasive.

Discovery sanctions under Federal Rule 37 are deterrents (specific and general) meant to punish a recalcitrant or evasive party. Nat'l Hockey League v. Metro. Hockey Club, Inc., 427 U.S. 639, 643 (1976); see Update Art, Inc. v. Modiin Publ'g, Ltd., 843 F.2d 67, 71 (2d Cir. 1988). A party might otherwise abuse or delay discovery, "embroil[ing] trial judges in day-to-day supervision." Cine Forty-Second St. Theatre Corp. v. Allied Artists Pictures Corp., 602 F.2d 1062, 1066 (2d Cir. 1979). "Without adequate sanctions the procedure for discovery would often be ineffectual," and the administration of justice would grind to a

halt. C. Wright & A. Miller, 8B Fed. Prac. & Proc. Civ. § 2281 (3d ed.). Federal Rule 37 protects more than the interest of a party in remedying or avoiding certain costs; it protects the interests of the parties, the court, and the public in a speedy and just resolution of the case.

To that end, Federal Rule 37 authorizes a range of sanctions, from mild to severe. In addition to precluding evidence, a district court may:

> (A) order payment of reasonable expenses, including attorney's fees, caused by the failure;
>
> (B) inform the jury of the party's failure; and
>
> (C) impose other appropriate sanctions, including any of the orders listed in Rule 37(b)(2)(A)(i)-(vi).

Fed. R. Civ. P. 37(c)(1). Federal Rule 37(b)(2)(A) authorizes "further just orders" against a party that disobeys a discovery order, such as dismissal of the action, default judgment, and contempt of court.

The bankruptcy court cites district court decisions imposing punitive monetary sanctions on counsel under that "just orders" clause. See, e.g., J. M. Cleminshaw Co. v. City of Norwich, 93 F.R.D. 338, 355 (D. Conn. 1981); see also Dissent at 15 (collecting cases). This Court has not decided whether such

sanctions are proper. In any event, Bankruptcy Rule 3002.1 lacks the authorization of "just orders." More importantly, the rule does not share the aims and functions of Federal Rule 37. Bankruptcy Rule 3002.1 protects a debtor's interest in fully resolving the debtor's current status as to particular financial obligations; Federal Rule 37 protects "the integrity of our judicial process" with an array of far harsher sanctions. Update Art, 843 F.2d at 73.

In the alternative, the Trustee argues that the $75,000 sanction is authorized under the bankruptcy court's inherent power. True, "bankruptcy courts, like Article III courts, possess inherent sanctioning powers," which "include[s] the power to impose relatively minor non-compensatory sanctions on attorneys appearing before the court in appropriate circumstances." Sanchez, 941 F.3d at 628. But while the bankruptcy court alluded to its inherent power, it did not assess whether the sanction was authorized under it; we cannot reach this question. See Kalikow, 602 F.3d at 96 ("[It is] imperative that the court explain its sanctions order with care, specificity, and attention to the sources of its power." (quoting Sakon v. Andreo, 119 F.3d 109, 113 (2d Cir.1997)). In any event, there is no finding of bad faith; so it is dubious that the bankruptcy court

could exercise its inherent power to do that which is unavailable under powers expressly defined. See Schlaifer Nance & Co. v. Estate of Warhol, 194 F.3d 323, 338 (2d Cir. 1999); see also Chambers v. NASCO, Inc., 501 U.S. 32, 47 (1991). The sanction was imposed under Rule 3002.1(i), and our holding is that the sanction went beyond the relief authorized by that rule.[2]

* * *

The dissent challenges our ruling on Rule 3002.1 and inherent power. If inherent power is alone sufficient to affirm the $75,000 sanction, there would be no reason to consider Rule 3002.1; so I begin there.

The dissent concedes that sanctions may only be imposed based on "specific authority invoked." Dissent at 26 (quoting Kalikow, 602 F.3d at 96).

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[2] The dissent argues that the bankruptcy court should be "afforded the opportunity to provide additional reasoning" on remand based on the dissent's assumption that the bankruptcy court imposed sanctions under its inherent power and just neglected to give reasons. Dissent at 31. Remand is appropriate when there is an error to fix, a new standard to apply, or, as the dissent emphasizes, further explanation needed of the decision that the court made. Here, the bankruptcy court simply did not exercise its inherent power to sanction PHH. The problem is not that the bankruptcy court's reasoning is too sparse for review. Our role is to review what the bankruptcy court did, not to survey options.

But the invocation identified by the dissent is no more than a perfunctory mention. That does not do. A court must justify the sanction in view of the specific source of its authority--especially when the source is inherent power. Inherent power is constrained: it requires "caution" and notice before use; and it is a last resort for when an express authority is not "up to the task." Chambers, 501 U.S. at 50. Although, as the dissent observes, the bankruptcy court analyzed cases on inherent power, it did so to decide what amount it should sanction *under Rule 3002.1*.

In any event, there is still the matter of bad faith. The dissent posits that the bankruptcy court found bad faith, at least more or less. Dissent at 31. When it came to the issue, the bankruptcy court said that PHH's actions "cannot realistically be attributed to an innocent mistake" and raised "serious concerns about whether PHH is making a good faith effort to comply with Rule 3002.1." Dissent at 30 (quoting Gravel I, 556 B.R. at 576 n.10). A concern, even a serious concern, is not a finding. So the dissent characterizes this concern, and associated "findings by the bankruptcy court of PHH's repeated violations," as constituting a finding that PHH's conduct was "tantamount to bad faith."

Dissent at 29–31. But tantamount means of the same weight; it does not mean lesser, and it is not a consolation prize. The dissent transmutes concern into a finding, and would thereby uphold sanctions on a basis that the bankruptcy court did not venture to make.

No wonder the dissent leans heavily on a non-finding to support the $75,000 sanction--PHH never charged the debtors a dime, and never collected a dime. The fees to which no notice was given were never due. The dissent fastidiously avoids acknowledging this little thing: the mortgage statements are said to have been "incorrect"; and they were "showing" fees. Dissent at 5, 7. On the final statements, the fees were $86.25 in the Beaulieu case, $371 in the Knisley case, and $258.75 in the Gravel case. Iterations of the same fees were re-listed on monthly statements in each case, none of them reflected in the amount due, and none of them paid. The rest is hyperventilation. It is surely of some matter there was no damage or harm here.

As for Rule 3002.1, the dissent's challenge proves too little. The dissent argues that the rule's sanction provisions have a deterrence function. Dissent at 17–20. True, but all sanctions deter, including compensatory ones; an award of

attorneys' fees, which compensates, simultaneously inflicts pain that is an incentive for compliance. In short, all sanctions "punish." Dissent at 2. The issue is whether the sanction must be calibrated to the prejudice. See Goodyear Tire & Rubber Co. v. Haeger, 137 S. Ct. 1178, 1186 (2017) (distinguishing compensatory from punitive sanctions). With respect to Rule 3002.1(i), the answer is yes.

The dissent is concerned that our interpretation of Rule 3002.1 "will undoubtedly hamper the ability of bankruptcy courts" to deter violations and protect debtors. Dissent at 2. But this concern is at best overwrought. The punitive sanction here is the first and only of its kind that a bankruptcy court has imposed in the over nine years since Rule 3002.1 was adopted. In any event, the majority opinion does not limit a bankruptcy court's inherent power to sanction offenders who act in bad faith. That is just not what the bankruptcy court did here; others might be free to do so if they were to make sufficient findings.

CONCLUSION

For the foregoing reasons, the order of the bankruptcy court is **VACATED** and **REVERSED**.

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE SOUTHERN DISTRICT OF TEXAS
BROWNSVILLE DIVISION

IN RE:	§	
RAMON BLANCO	§	**CASE NO: 20-10078**
and	§	
MARIA P BLANCO,	§	**CHAPTER 13**
Debtors.	§	
	§	
RAMON BLANCO	§	
and	§	
MARIA P BLANCO,	§	
Plaintiffs,	§	
	§	
VS.	§	**ADVERSARY NO. 20-1005**
	§	
BAYVIEW LOAN SERVICING LLC,	§	
Defendant.	§	

MEMORANDUM OPINION

Plaintiffs Ramon and Maria P. Blanco filed an adversary proceeding, incorporating their previously filed claim objection, and asserting core bankruptcy claims such as lien avoidance and violations of Rule 3002.1, the automatic stay, and the discharge injunction, to name a few. The target of the complaint is Defendant Community Loan Servicing, LLC f/k/a Bayview Loan Servicing, LLC who responded with a motion seeking partial dismissal of Plaintiffs' complaint for failure to state a claim. Not to be outdone, Plaintiffs filed their own motion seeking dismissal of Defendant's counterclaims and for entry of a judgment on the pleadings.

On September 7, 2021, the Court held a hearing on the competing motions and for the reasons set forth herein, Ramon and Maria P. Blanco's Counts I and II are dismissed with prejudice, their motion for judgment on the pleadings is denied and their request for leave to amend their complaint is denied. Community Loan Servicing, LLC f/k/a Bayview Loan Servicing, LLC's Count II is dismissed, and their request for leave to amend its answer and counterclaims is denied.

I. BACKGROUND

A. Procedural History

In Ramon and Maria P. Blanco's ("*Plaintiffs*") underlying bankruptcy case, Community Loan Servicing, LLC f/k/a Bayview Loan Servicing, LLC ("*Defendant*") filed a proof of claim. As discussed below, that proof of claim has been amended twice. Plaintiffs filed an objection to Defendant's proof of claim, later incorporating that objection into an original complaint, and asserting several claims ("*Complaint*").[1]

Plaintiffs' Complaint sets forth nine causes of action: (i) Defendant's lien is void under Texas law; (ii) avoidance of loan and lien; (iii) violations of Federal Rule of Bankruptcy Procedure 3002.1; (iv) objection to Defendant's proof of claim; (v) violation of the plan and the order confirming the plan; (vi) willful violation of the automatic stay pursuant to 11 U.S.C. § 362(a)(3); (vii) violation of the discharge injunction pursuant to 11 U.S.C. § 524(i); (viii) contempt, and (ix) breach of contract Plaintiffs also seek injunctive relief and request actual, statutory, and punitive damages, plus attorney's fees and sanctions.[2] Plaintiffs' claims against Defendant arise from a prior bankruptcy case, 11-70475, that was discharged by this Court in 2018 ("*2011 Case*") and the instant bankruptcy proceeding.

Defendant filed an answer to Plaintiffs' Complaint and alleged two counterclaims for breach of contract and declaratory judgment.[3] Defendant then filed, and later amended, a partial motion to dismiss Plaintiffs' Complaint for failure to state a claim ("*Motion to Dismiss*").[4] Plaintiffs filed their competing "Motion to Dismiss Defendant's Counterclaims for Failure to State a Claim and Motion for Judgment on the Pleadings" ("*Plaintiffs' Motion*").[5] Each party timely filed

[1] ECF No. 21.
[2] *Id.*
[3] ECF No. 23.
[4] ECF No. 34.
[5] ECF No. 36.

the appropriate responses and replies to the cross-motions to dismiss.[6] On September 7, 2021, the Court held a hearing on the Motions.

B. Factual Background

1. The $68,000 Note and accompanying Deed of Trust

The factual background in this case spans two decades and is highly contested. In this section, the Court details undisputed facts, unless otherwise noted.

Plaintiffs own the real property at issue in this case, 4015 E. Expressway 83, Weslaco, Texas 78596 having a legal description of: Lot Seven (7), Dellinger Subdivision, an Addition to the City of Mercedes, Hidalgo County, Texas, as per map or plat thereof recorded in Volume 22, Page 39, Map Records, Hidalgo County, Texas ("*Property*").[7] In 2001, Plaintiffs took out a loan on the Property from InterBay Funding, LLC ("*InterBay*"), executing a note for $68,000 ("*Note*") and a corresponding deed of trust ("*Deed of Trust*").[8] Through a series of assignments that Plaintiffs allege were defective, InterBay' s interest in the Note and Deed of Trust was purportedly transferred to Defendant.[9]

On January 25, 2010, Plaintiff Ramon Blanco and Defendant executed a Modification Agreement of the Note and Deed of Trust ("*Modification Agreement*"). The Modification Agreement restructured the Note and raised it to an unpaid principal balance due of $115,340.64 and provided for monthly payments of $1,197.40.[10]

2. Plaintiffs' 2011 bankruptcy case

On August 1, 2011, Plaintiffs filed a bankruptcy petition, initiating the 2011 Case. Cindy

[6] ECF No. 37 (Plaintiffs' response to Defendant's Motion to Dismiss); ECF No. 38 (Defendant's Reply); ECF No. 40 (Defendant's response to Plaintiffs' Motion to Dismiss); ECF No. 42 (Plaintiffs' Reply).
[7] ECF No. 1 at 6, ¶ 12.
[8] ECF No. 21 at 7, ¶ 21; ECF No. 23 at 4, ¶ 21.
[9] ECF No. 21 at 8–10, ¶¶ 29–37, 40–43.
[10] ECF No. 21 at 10, ¶ 38; ECF No. 23 at 5, ¶ 38.

Boudloche was the chapter 13 trustee ("*Trustee*").[11] Defendant filed a proof of claim ("*2011 POC*") in the 2011 Case for $124,157.54 and listed $16,052.69 in arrears and an on-going mortgage payment of $1,197.40.[12] Plaintiffs' reorganization plan proposed to pay the $1,197.00 through the Trustee. The plan also proposed to pay the arrears with 5.252% interest.[13] That plan was confirmed.[14]

On November 30, 2011, Defendant filed a Notice of Mortgage Payment Adjustment ("*NPC*"), notifying all parties that the monthly payment would increase to $1,251.57 effective January 1, 2012. Plaintiffs did not object to the NPC.[15] On December 21, 2011, Defendant filed a Motion to Lift Stay, wherein it represented that the on-going monthly mortgage payments were $1,197.40.[16] On January 27, 2012, this Court entered an Agreed Order resolving the Lift Stay motion.[17] The Agreed Order stated that Plaintiffs were to continue paying $1,197.40, not the amount reflected in the November 30, 2011 NPC.[18] On December 29, 2011, the Trustee filed a Trustee's Report,[19] notifying Defendant that:

> According to the Trustee's records, the current monthly mortgage payment is $1,197.40. Written notice of changes in the monthly payment must be provided to the Trustee, the Debtor and Debtor's counsel 21 days prior to the effective date of the mortgage payment change, pursuant to Bankruptcy Rule 3002.1(b). [20]

Four years later, Plaintiffs filed an Amended Motion to Modify their chapter 13 plan ("*2011 Plan*") to allow for the claim of a non-related creditor; however, therein, Plaintiffs proposed to continue paying Defendant on its claim the amount of $1,197.40 until the end of the plan.

[11] ECF No. 21 at 11-12, ¶ 52; ECF No. 23 at 6, ¶ 52.
[12] ECF No. 21 at 12, ¶ 54; ECF No. 23 at 7, ¶ 54.
[13] ECF No. 21 at 12, ¶ 53; ECF No. 23 at 6, ¶ 53.
[14] 11-70475, ECF No. 67.
[15] ECF No. 21 at 12 ¶ 56; ECF No. 23 at 7, ¶ 56.
[16] ECF No. 21 at 12–13, ¶ 57; ECF No. 23 at 7, ¶ 57.
[17] 11-70475, ECF No. 91.
[18] ECF No. 21 at 12-13, ¶ 57; ECF No. 23 at 7, ¶ 57.
[19] ECF No. 21 at 13, ¶ 58; ECF No. 23 at 7, ¶ 58.
[20] ECF No. 21 at 13, ¶ 59; ECF No. 23 at 7, ¶ 59.

Defendant did not object to the Modification.[21] The Court granted Plaintiffs' Amended Motion to Modify. The Trustee made all the mortgage payments to Defendant in the amount of $1,197.40, totaling $71,898.17 over the sixty months of the 2011 Plan. The Trustee also paid all the pre-petition arrearage.[22]

On September 29, 2016, the Trustee filed a Motion to Deem the Mortgage Current under Federal Rule of Bankruptcy Procedure 3002.1(f). In it, the Trustee stated that the monthly mortgage payment in her books and records as of that date was $1,197.40. The Trustee also stated that the "Next Payment Due Date" was September 2016.[23] On October 5, 2016, Defendant filed a Form 4100R Response to Notice of Final Cure Payment under Federal Rule of Bankruptcy Procedure 3002.1(g).[24] Therein, Defendant agreed with the Trustee that: (1) Plaintiffs cured the pre-petition default on Defendant's claim; (2) "[Plaintiffs] are current with all post-petition payments consistent with §1322(b)(5) of the Bankruptcy Code, including all fees, charges, expenses, escrow, and costs; and (3) the next payment due date was September 1, 2016. Defendant did not object to the monthly payment amount of $1,197.40.[25]

On October 11, 2016, this Court signed an Order Deeming Mortgage Current and Directing Debtors to Resume Payments ("*Deem Current Order*"). In that order, this Court found that all payments to Defendant under the confirmed plan were completed and that "(i) the claims of the above-listed creditor(s) (Community) are deemed current; (ii) all escrow deficiencies, if any, are deemed cured; and (iii) all legal fees, inspection fees and other charges imposed by the creditor, if any, are deemed satisfied in full as of the next payment due date set forth below and that the

[21] ECF No. 21 at 13, ¶ 60; ECF No. 23 at 7, ¶ 60.
[22] ECF No. 21 at 13, ¶ 61; ECF No. 23 at 7, ¶ 61.
[23] ECF No. 21 at 14, ¶ 62; ECF No. 23 at 7, ¶ 62.
[24] 11-70475, ECF No. 206.
[25] ECF No. 21 at 14, ¶ 63; ECF No. 23 at 7, ¶ 63.

creditor shall be solely responsible for any shortfall or failure to respond to the Trustee's notice and motion."[26] Further, the Order directed Plaintiffs pay $1,197.40 directly to Defendant beginning September 2016.[27]

On October 20, 2016, the Trustee filed a Notice of Plan Completion.[28] Despite that Notice and this Court's Deem Current Order, Defendant filed an NPC under Official Form 410S1, after the 2011 Plan had been completed and was no longer in effect.[29] The NPC indicated that the mortgage payment would increase to $2,012.00 effective March 1, 2017 based on an alleged increase in the escrow payment from $627.69 to $1,185.69. Plaintiffs did not object to the NPC, allegedly because the 2011 Plan had been completed and was no longer in effect.[30]

On May 31, 2017, the Trustee withdrew her Notice of Plan Completion.[31] Thereafter, the Trustee filed an updated Notice, stating that all "plan payments were properly adjusted to reflect any change in mortgage payments after confirmation or the last approved modification." Defendant did not object to the Trustee's updated Notice.[32] On September 13, 2018, this Court granted Plaintiffs a discharge and entered a Final Decree.[33]

3. Defendant's attempt to foreclose

Plaintiffs admit that they stopped making payments to Defendant in November 2018, allegedly because they grew frustrated with Defendant's post-discharge activities, recounted throughout this Memorandum Opinion.[34] Defendant notified Plaintiffs of its intent to foreclose on

[26] 11-70475, ECF No. 207.
[27] ECF No. 21 at 14, ¶ 64; ECF No. 23 at 7, ¶ 64.
[28] ECF No. 21 at 14, ¶ 65; ECF No. 23 at 7, ¶ 65.
[29] ECF No. 21 at 15, ¶ 66; ECF No. 23 at 7, ¶ 66.
[30] ECF No. 21 at 15, ¶ 67; ECF No. 23 at 7, ¶ 67.
[31] ECF No. 21 at 15, ¶ 68; ECF No. 23 at 7, ¶ 68.
[32] ECF No. 21 at 15, ¶ 69; ECF No. 23 at 7, ¶ 69.
[33] ECF No. 21 at 15, ¶ 70; ECF No. 23 at 8, ¶ 70.
[34] ECF No. 21 at 15–16, ¶ 71.

the Property and scheduled a foreclosure sale for August 6, 2019.[35] Plaintiffs filed a state court action in Hidalgo County on July 30, 2019 to stop the foreclosure.[36] Defendant removed the state court proceeding to federal court and the Plaintiffs voluntarily dismissed the case.[37]

4. Plaintiffs' instant bankruptcy case

On February 27, 2020, Plaintiffs filed their initial petition and schedules under chapter 13 of title 11 of the United States Code, initiating the instant bankruptcy case.[38] Plaintiffs scheduled Defendant as having a claim secured by a first lien mortgage on the Property.[39] Defendant filed a proof of claim and has twice amended that claim. The amended proof of claim currently before the Court is Claim No. 9-3.[40] Claim No. 9-3 is comprised of the following:

a. Monthly mortgage payment in the amount of $1,453.39;
b. Outstanding principal of $103,483.49;
c. Default interest of $12,142.60;
d. Fees and costs due of $6,865.97;
e. Escrow deficiency funds of $3,212.69; and
f. Less total funds on hand of $355.37
g. Total debt $132,678.08

The $33,607.60 arrearage component of the claim is comprised of the following:

h. Principal and interest due of $21,375.97;
i. Pre-petition fees due of $6,865.97;
j. Escrow deficiency for funds advanced of $3,212.69;
k. Projected Escrow shortage of $2,508.34; and
l. Less total funds on hand of $355.37.[41]

[35] ECF No. 21 at 17, ¶ 78; ECF No. 23 at 8, ¶ 78.
[36] ECF No. 21 at 17, ¶ 79; ECF No. 23 at 8, ¶ 79.
[37] ECF No. 21 at 17, ¶ 79; ECF No. 23 at 8, ¶ 79.
[38] Any reference to "Code" or "Bankruptcy Code" is a reference to the United States Bankruptcy Code, 11 U.S.C., or any section (i.e.§) thereof refers to the corresponding section in 11 U.S.C. "Bankr. ECF" refers docket entries made in the Debtors' bankruptcy case, No. 20-10078. Entries made in Plaintiffs' 2011 Case take the format 11-70475, ECF No. __.
[39] ECF No. 21 at 10, ¶ 45; ECF No. 23 at 6, ¶ 45.
[40] ECF No. 21 at 11, ¶ 46; ECF No. 23 at 6, ¶ 46.
[41] ECF No. 21 at 11, ¶ 51; ECF No. 23 at 6, ¶ 51.

II. JURISDICTION AND VENUE

This Court holds jurisdiction pursuant to 28 U.S.C. § 1334, which provides "the district courts shall have original and exclusive jurisdiction of all cases under title 11." Section 157 allows a district court to "refer" all bankruptcy and related cases to the bankruptcy court, wherein the latter court will appropriately preside over the matter.[42] This court determines that pursuant to 28 U.S.C. § 157(b)(2)(A), (B), (K), and (L), this adversary proceeding contains core matters because the complaint primarily asserts claims and seeks relief under the United States Bankruptcy Code, including contempt and sanctions for violation of their chapter 13 Plan, the confirmation order, and violations of Federal Rule of Bankruptcy Procedure 3002.1, and 11 U.S.C. § 524(i).[43]

Furthermore, this Court may only hear a case in which venue is proper.[44] Pursuant to 28 U.S.C. § 1409(a), "a proceeding arising under title 11 or arising in or related to a case under title 11 may be commenced in the district court in which such case is pending." Plaintiffs' chapter 13 case is presently pending in this Court and therefore, venue of this adversary proceeding is proper.

III. CONSTITUTIONAL AUTHORITY

This Court must evaluate whether it has constitutional authority to enter a final judgment in this case. In *Stern,* which involved a core proceeding brought by the debtor under 28 U.S.C. § 157(b)(2)(C), the Supreme Court held that a bankruptcy court "lacked the constitutional authority to enter a final judgment on a state law counterclaim that is not resolved in the process of ruling on a creditor's proof of claim."[45] However, *Stern* is inapplicable to the instant case. *Stern* concerned final orders entered by the bankruptcy court and here, the Court need only enter an

[42] 28 U.S.C. § 157(a); *see also* In re: Order of Reference to Bankruptcy Judges, Gen. Order 2012-6 (S.D. Tex. May 24, 2012).
[43] *See* 28 U.S.C. § 157(b).
[44] 28 U.S.C. § 1408.
[45] *Stern v. Marshall*, 564 U.S. 462, 503 (2011).

interlocutory order because motions to dismiss pursuant to Federal Rule of Civil Procedure ("*FRCP*") 12(b)(6), like the instant motions filed by Defendant and Plaintiffs, are interlocutory. Entering an interlocutory order does not implicate "the constitutional limitations on the Court's authority to enter final judgments."[46] Therefore, this Court need not determine whether it has constitutional authority to enter a final judgment because an interlocutory order is all the instant case requires.[47]

IV. ANALYSIS

A. Defendant's Motion to Dismiss

Under FRCP 12(b)(6), this Court may dismiss a complaint for "failure to state a claim upon which relief can be granted."[48] However, motions to dismiss are disfavored and therefore, rarely granted.[49] This Court reviews motions under FRCP 12(b)(6) by "accepting all well-pleaded facts as true and viewing those facts in the light most favorable to the plaintiffs."[50] Although this Court "will not strain to find inferences favorable to the plaintiff,"[51] the facts need only be sufficient "for an inference to be drawn that the elements of the claim exist."[52]

To defeat a motion to dismiss pursuant to FRCP 12(b)(6), a plaintiff must meet FRCP 8(a)(2)'s pleading requirements. FRCP 8(a)(2) requires a plaintiff to plead "a short and plain statement of the claim showing that the pleader is entitled to relief."[53] In *Ashcroft v. Iqbal*, the

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[46] *West v. WRG Energy Partners LLC (In re Noram Res., Inc.)*, 2011 Bankr. LEXIS 5183, at *3 (Bankr. S.D. Tex. Dec. 30, 2011).
[47] *See Shelton v. Aguirre & Patterson, Inc. (In re Shelton)*, 2014 Bankr. LEXIS 1722, at *11 (Bankr. S.D. Tex. Apr. 18, 2014) (explaining that a bankruptcy court may not dismiss a cause of action with prejudice because that would constitute adjudication on the merits and thus a final order dismissing the plaintiff's suit. However, the court continued, a court may issue an interlocutory order even where it does not have authority to enter a final order.)
[48] FED. R. CIV. P. 12(b)(6).
[49] *Test Masters Educ. Servs., Inc. v. Singh*, 428 F.3d 559, 570 (5th Cir. 2005).
[50] *Stokes v. Gann*, 498 F. 3d 483, 484 (5th Cir. 2007) (per curiam).
[51] *Southland Sec. Corp. v. INSpire Ins. Solutions Inc.,* 365 F.3d 353, 361 (5th Cir. 2004) (internal quotations omitted).
[52] *Harris v. Fidelity Nat'l Info. Serv* (*In re Harris*), 2008 Bankr. LEXIS 1072, at *11 (Bankr. S.D. Tex. Apr. 4, 2008) (citing *Walker v. South Cent. Bell Tel. Co*., 904 F2d 275, 277 (5th Cir. 1990)).
[53] FED. R. CIV. P. 8(a).

Supreme Court held that FRCP 8(a)(2) requires that "the well-pleaded facts . . . permit the court to infer more than the mere possibility of misconduct."[54] "Only a complaint that states a plausible claim for relief survives a motion to dismiss."[55] "A claim has facial plausibility when the plaintiff pleads factual content that allows the court to draw the reasonable inference that the defendant is liable for the misconduct alleged."[56] "The plausibility standard is not akin to a 'probability requirement,' but it asks for more than a sheer possibility that a defendant has acted unlawfully."[57]

In its Motion to Dismiss, Defendant alleges:

1. Plaintiffs' Counts I and II should be dismissed because Plaintiffs' challenges to the validity of the Note and Deed of Trust securing Defendant's lien:

    a. are barred by the doctrines of judicial estoppel and *res judicata* because of this Court's Orders and Plaintiffs' actions in their 2011 Case; and

    b. even if Count II is not barred by either doctrine, Plaintiffs lack standing to challenge the validity of the assignments of the Note and Deed of Trust to which they were not a party;

2. Plaintiffs' Count III should be dismissed because Federal Rule of Bankruptcy Procedure 3002.1 does not provide a basis for an independent cause of action in this case, and Plaintiffs have not alleged damages by virtue of the alleged violations in their previous bankruptcy proceeding; and

3. Plaintiffs' Counts V–VIII should be dismissed because Plaintiffs have not alleged any specific damages resulting from Defendant's alleged violation of any of this Court's Orders.[58]

The Court considers each in turn.

1. Plaintiffs' Counts I (void lien) and II (avoidance of loan and lien)

[54] 556 U.S. 662, 679, (2009) (quoting FED. R. CIV. P. 8(a)(2)).
[55] *Id*. (citing *Twombly*, 550 U.S. at 556 (2007)).
[56] *Id.* at 678 (citing *Twombly,* 550 U.S. at 555).
[57] *Id*. (quoting *Twombly*, 550 U.S. at 556). *See also Lormand v. US Unwired, Inc*., 565 F.3d 228, 232 (5th Cir. 2009) (citations omitted) ("A complaint does not need detailed factual allegations but must provide the plaintiff's grounds for entitlement to relief – including factual allegations that when assumed to be true raise a right to relief above the speculative level.").
[58] ECF No. 34 at 5.

In Count I, Plaintiffs allege that Defendant's asserted lien is unenforceable against Plaintiffs' Property under Texas law, including but not limited to section 50 of the Texas Constitution, because the loan is a commercial loan secured by a lien on a homestead.[59] Under Texas law, a homestead is protected against all debts except for purchase money and specified improvements. Article XVI, section 50 of the Texas Constitution provides, in pertinent part:

> The homestead of a family . . . is hereby protected from forced sale for the payment of all debts except for the purchase money thereof, or a part of such purchase money, the taxes due thereon, or for work and material used in constructing improvements thereon . . . . No mortgage, trust deed, or other lien on the homestead shall ever be valid unless it secures a debt described in this section . . . . All pretended sales of the homestead involving any condition of defeasance shall be void.[60]

Plaintiffs' Complaint alleges that (i) they have resided at the Property since acquiring it in 1994 and they have never given up their intent to treat the property as their homestead; (ii) the original lender, InterBay, by and through its funding agent, Mr. Bocanegra, knew that the Plaintiffs resided on the Property at the time it extended the loan; (iii) InterBay' s own mortgage application states it is a residential application and not a commercial application; and (iv) Plaintiffs filed a Homestead Designation in Hidalgo County, Texas in 2014, designating the Property as their homestead.[61]

In Count II, Plaintiffs allege that Defendant's secured claim should be disallowed in its entirety under 11 U.S.C. §506 because Defendant (i) does not hold a valid lien on the Property under Texas law; and (ii) has no contractual standing to assert the claim because it is not the holder of the Note. Plaintiffs allege that Defendant is not the holder of the lien because the three assignments purportedly transferring InterBay's interest in the Note and Deed of Trust to Defendant were defective for the reasons discussed below.

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[59] ECF No. 21 at 19, ¶ 88.
[60] TEX. CONST. art. 16, §§ 50(a)(1)–(3), (c).
[61] ECF No. 21 at 19, ¶ 88.

a. Whether Plaintiffs have standing to challenge the validity of assignments of the Note and Deed of Trust

Defendant's third basis for dismissal of Plaintiffs' Count II challenges Plaintiffs' standing. Because standing is a threshold matter, the Court analyzes this issue first.[62] Defendant insists that Plaintiffs lack standing to challenge the validity of the assignments of the Note and Deed of Trust because Plaintiffs were not parties to any of the assignments in question.[63]

Plaintiffs retort that they do have standing and distinguish the present case from *Crymes*,[64] a case cited by Defendant. Plaintiffs argue that this case differs from *Crymes* in three important respects: (1) here, Defendant's proof of claim constitutes a complaint and Plaintiffs' objection constitutes an answer, unlike in *Crymes* where the plaintiff launched an offensive attack challenging the validity of the creditor's lien; (2) the assignments in *Crymes* were facially valid, but here the alleged "extensive deficiencies" are "facially obvious"; and (3) the secured creditor in *Crymes* did not file a proof of claim, preferring its lien to pass through bankruptcy under § 506(d)(2) whereas here, Defendant filed a proof of claim, attaching one of the deficient assignments, and Plaintiffs are within their rights to challenge that proof of claim and asserted lien.[65]

i. Plaintiffs' challenge to the assignments constitutes a defense to Defendant's Claim No. 9-3

Standing under Texas law "focuses on whether a party has a sufficient relationship with a lawsuit so as to have a justiciable interest in its outcome."[66] If a party was personally aggrieved by an alleged wrong, then it has standing to sue.[67] Conversely, if the party does not have a legal right belonging to it, then it does not have standing to sue.[68] A mortgagor's standing to challenge

[62] ECF No. 34 at 17–18.
[63] ECF No. 34 at 18.
[64] 2018 Bankr. LEXIS 2479 (Bankr. N.D. Tex. Aug. 20, 2018).
[65] ECF No. 37 at 16–17.
[66] *Austin Nursing Ctr., Inc. v. Lovata*, 171 S.W.3d 845, 848 (Tex. 2005).
[67] *Nootsie, Ltd. v. Williamson County Appraisal Dist.*, 925 S.W.2d 659, 661 (Tex. 1996).
[68] *Nobles v. Marcus*, 533 S.W.2d 923, 927 (Tex. 1976).

assignments of a deed of trust lien that secures a debt to which the mortgagor was not a party is limited.[69] Plaintiffs have not alleged that they are parties to the assignments. Thus, if Plaintiffs' success on the merits would merely render the allegedly deficient assignments voidable, then Plaintiffs do not have standing to challenge those assignments.[70] If Plaintiffs' success would render the assignments void, then Plaintiffs do have standing to challenge Defendant's efforts to enforce the lien based on the assignments.[71]

The basis of Plaintiffs' first and third arguments is that they have standing to challenge the assignments because they are merely defending against Defendant's Claim No. 9-3 by disputing its secured status under § 506.[72] Plaintiffs cite *Continental Airlines* for the proposition that Defendant's proof of claim acts as an original complaint and Plaintiffs' objection is an answer to that complaint.[73] There, the Fifth Circuit said, "[a]s we stated in *In re Simmons*, 765 F.2d 547 (5th Cir. 1985), the filing of a proof of claim is analogous to the filing of a complaint in a civil action, with the bankrupt's objection the same as the answer."[74] In *Simmons*, the Fifth Circuit held that "[t]he objection to a claim initiates a contested matter unless the objection is joined with a counterclaim asking for the kind of relief specified in Bankruptcy Rule 7001."[75]

[69] *See, e.g.*, *Ferguson v. Bank of N.Y. Mellon Corp.*, 802 F.3d 777, 780–81 (5th Cir. 2015) ("Borrowers have limited standing to challenge their lenders' assignments of their promissory notes and DOTs. In Texas an obligor cannot defend against an assignee's efforts to enforce the obligation on a ground that merely renders the assignment *voidable* at the election of the assignor." But an obligor has standing to challenge an assignee's efforts to enforce the obligation on a ground that would render the assignment *void*. Therefore, the [obligors] have standing to challenge the [assignee's] efforts to foreclose if the [obligor's] claim would render the assignment void rather than voidable.") (cleaned up).
[70] *Id.*
[71] *Id.*
[72] ECF No. 37 at 16.
[73] *Id.* (citing *In re Continental Airlines*, 928 F.2d 127, 129 (5th Cir. 1991)).
[74] *In re Continental Airlines*, 928 F.2d at 129.
[75] 765 F.2d at 552.

The relief specified in Rule 7001 includes proceedings to recover money, determine the validity of a lien, and obtain an injunction.[76] Plaintiffs' Complaint seeks all three.[77] As noted in *Express One*, an objection joined with a counterclaim to recover money becomes an adversary proceeding pursuant to Rule 3007.[78] Rule 3007 states, "[a] party in interest shall not include a demand for relief of a kind specified in Rule 7001 in an objection to the allowance of a claim, but may include the objection in an adversary proceeding."[79]

Here, Plaintiffs filed an objection to Defendant's Claim No. 9-2, since amended to Claim No. 9-3, in the underlying bankruptcy case ("*Objection*"). In that Objection, Plaintiffs contested, inter alia, Defendant's secured status, arguing that Defendant does not hold a valid lien under Texas law, and sought disallowance of the claim under § 506.[80] Plaintiffs orally requested that certain adversary proceeding rules be applied to their Objection.[81] That request was granted.[82] Thereafter, this Court entered a scheduling order, requiring Plaintiffs to file a complaint.[83] Plaintiffs' Complaint reiterated their challenge to Defendant's secured status, but added several claims, including an additional challenge to the validity of Defendant's lien based on the Texas Constitution.[84]

Pursuant to *Continental Airlines*, the Objection constituted an answer to Defendant's Claim No. 9-3.[85] Plaintiffs' Complaint incorporated the arguments made in their Objection and lodged

[76] FED. R. BANKR. P. 7001(1)–(2), (7). *See also id.* 3007(b) ("A party in interest shall not include a demand for relief of a kind specified in Rule 7001 in an objection to the allowance of a claim, but may include the objection in an adversary proceeding.").
[77] ECF No. 21 at 19–22 (validity of lien), 36–37 (injunctive relief and damages).
[78] *In re Express One Int'l*, 243 B.R. 290, 292 (Bankr. E.D. Tex. 1999).
[79] FED. R. BANKR. P. 3007(b).
[80] 20-10078, ECF No. 98.
[81] See 20-10078, November 12, 2020 Min. Entry; 20-1005, ECF No. 1.
[82] ECF No. 1.
[83] ECF No. 12.
[84] ECF No. 21.
[85] 928 F.2d at 129.

additional claims.[86] Despite their inclusion in Plaintiffs' Complaint, Plaintiffs' objections to Defendant's Claim No. 9-3 substantively constitute an answer to Defendant's Claim No. 9-3.[87] Because that portion of Plaintiffs' Complaint is a responsive pleading, Plaintiffs' challenge to the assignments is a defense to Defendant's Claim No. 9-3. Nonetheless, for Plaintiffs to have standing, that defense must render the assignments void, not merely voidable.[88]

ii. Plaintiffs' challenge to the assignments of the Note and Deed of Trust would not render the assignments void

Plaintiffs argue that Defendant must prove "successive transfer of possession and indorsement establishing an unbroken chain of title" to enforce the Note as a holder.[89] Plaintiffs also complain that Defendant is not the legal holder of the Deed of Trust lien because of the three allegedly defective assignments. Specifically, Plaintiffs allege that: (1) the first assignment was not recorded and is defective because it does not list an assignee;[90] (2) the second assignment, from InterBay to Bayview, is defective because it is not an original document and is a clear manipulation of the first assignment, containing false representations as to the execution date of the assignment;[91] and (3) the third assignment is defective because it was signed by Defendant, not by the true owner of the Deed of Trust, InterBay Funding, LLC.[92] Plaintiffs attach copies of all three

[86] *Compare* 20-10078, ECF No. 98, *with* ECF No. 21. *See also* ECF No. 21 at 5 ("The Blancos have filed this complaint to object to Community's claim, both as a secured claim, because the liens are defective and in violation of Plaintiffs' homestead rights under Texas law, and as to the amount of the claim.").
[87] *See, e.g.*, *Continental Airlines*, 928 F.2d at 129; *In re Simmons*, 765 F.2d at 552 (citing *Nortex Trading Corp. v. Newfield*, 311 F.2d 163, 164 (2d Cir. 1962) ("The filing by Nortex of its proof of claim is analogous to the commencement of an action within the bankruptcy proceeding. The trustee's petition is in the nature of an answer incorporating an affirmative request for relief by way of surrender of the preference.")).
[88] *See Murphy v. HSBC Bank USA*, 2017 U.S. Dist LEXIS 11948, at *17 (S.D. Tex. Jan. 30, 2017) ("The law is settled that the obligors of a claim may defend the suit brought thereon on any ground which renders the assignment void, but may not defend on any ground which renders the assignment voidable only, because the only interest or right which an obligor of a claim has in the instrument of assignment is to insure himself that he will not have to pay the same claim twice.") (quoting *Calderon v. Bank of America*, 941 F. Supp. 2d 753, 764 (W.D. Tex. 2013)).
[89] ECF No. 21 at 20–21 (citing *Miller v. Homecomings Fin., LLC*, 881 F. Supp. 2d 825, 827, 831–32 (S.D. Tex. 2012)).
[90] *Id.* at 9, ¶¶ 31–32.
[91] *Id.* ¶¶ 33–37.
[92] *Id.* at 10, ¶¶ 40–43.

assignments to their Complaint.[93] As explained below, Plaintiffs' challenges to the assignments are flawed for several reasons.

The first assignment

Plaintiffs' reference to their Exhibit D[94] as the "first assignment" is somewhat of a misnomer. That document refers to the Property and Plaintiffs by name, but it does not designate an assignee and does not contain a recording stamp.[95] Pursuant to Texas Property Code section 13.001 an unrecorded instrument binds the parties to that instrument and their heirs.[96] Because there is no assignee here, there are no parties to bind. The "first assignment" is merely an incomplete document and thus, not void or voidable. Therefore, Plaintiffs lack standing to challenge the so-called first assignment.

The second assignment

Plaintiffs offer the first assignment to demonstrate that the second assignment, Exhibit E,[97] is deficient because it is a manipulation of the first assignment and was modified after notarization.[98] Specifically, Plaintiffs complain that the signatures of the assignor, the witnesses, and the notary, plus the date of execution and notarization on the second assignment are identical to those on the first, but that the second assignment contains handwritten changes not included on the first assignment.[99]

Taking as true that these deficiencies establish a "manipulation" of the first assignment, Plaintiffs provide no legal support for the proposition that a manipulation of a previously

[93] ECF Nos. 21-4, 21-5, 21-7. The Court may review any documents attached to the complaint when deciding a FRCP 12(b)(6) motion. *Lone Star Fund V (US), LP v. Barclays Bank PLC*, 594 F.3d 383, 387 (5th Cir. 2010).
[94] ECF No. 21-4.
[95] *Id.*
[96] TEX. PROP. CODE § 13.001(b).
[97] ECF No. 21-5.
[98] ECF No. 21 at 9, ¶¶ 36–37.
[99] *Id.* ¶¶ 35–36.

incomplete and unrecorded assignment makes the second assignment void. Moreover, "manipulation" is not a legal basis on which an assignment can be challenged. There is either fraud or forgery.[100] Texas law is clear that a homeowner does not have standing to challenge an assignment based on fraud because any claim of fraud belongs to the grantor of the assignment, rather than to the third-party homeowner.[101] Conversely, a homeowner has standing to challenge an assignment based on forgery because a forged instrument is void.[102] This Court cannot determine whether Plaintiffs' Complaint is alleging fraud or forgery or neither and thus, cannot determine whether Plaintiff has standing to challenge the second assignment as void.

To the extent Plaintiffs complain that the document was modified after being notarized and "therefore is not a sworn statement as to the modifications thereon,"[103] Plaintiffs provide no controlling law that requires an assignment to be notarized. Under Texas law, a mortgage assignment must be notarized for recording, but Texas's recording statute protects subsequent purchasers for value and without notice.[104] Errors in the notarization of the assignment may prevent Defendant from enforcing the Note and Deed of Trust against a third party who purchased the Property from Plaintiffs without actual knowledge of the mortgage, but it does not affect Defendant's rights against Plaintiffs.[105]

While Plaintiffs may have standing to challenge the second assignment based on forgery, Plaintiffs have not alleged facts from which this Court can conclude that Plaintiffs are bringing such a claim. Thus, because "manipulation" is not a legal basis on which an assignment can be

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[100] *Everbank v. Seedergy Ventures, Inc.*, 499 S.W.3d 534, 542 (Tex. App.—Houston [14th Dist.] 2016, no pet.).
[101] *Id.*
[102] *Id.* (citing *Vazquez v. Deutsche Bank Nat'l Trust Co.*, 441 S.W.3d 783, 787 (Tex. App.—Houston [1st Dist.] 2014, no pet.)).
[103] ECF No. 21 at 9, ¶ 37.
[104] *Reinagel v. Deutsche Bank Nat'l Trust Co.*, 735 F.3d 220, 227 (5th Cir. 2013) (citing TEX. PROP. CODE §§ 12.001(b), 13.001(a)).
[105] *See id.*

challenged and improper notarization does not affect Defendant's rights against Plaintiffs, Plaintiffs lack standing to challenge the second assignment.

The third assignment

Plaintiffs' final flawed argument is that the third assignment was not filed in the same manner as the original instrument as required by Texas Local Government Code section 192.007(a) because it was signed by Defendant, not InterBay Funding, LLC, the alleged valid holder of the Deed of Trust.[106] Texas Local Government Code section 192.007(a) provides:

> To release, transfer, assign, or take another action relating to an instrument that is filed, registered, or recorded in the office of the county clerk, a person must file, register, or record another instrument relating to the action in the same manner as the original instrument was required to be filed, registered, or recorded.

It is well settled that "the absence of recordation in compliance with section 192.007 of the Texas Local Government Code 'does not affect the validity of the assigned deed of trust *between the homeowner and the lender*.'"[107] Rather, that section "is best read as a procedural directive to county clerks, not as a prerequisite to the validity of assignments."[108]

Plaintiffs also allege that Defendant "in essence, attempted to assign the Deed of Trust to itself."[109] That allegation is factually inaccurate on the face of the third assignment attached to the Complaint at Exhibit G.[110] Wachovia Bank, N.A., as Indenture Trustee (Bayview), was the

ASSIGNOR: **WACHOVIA BANK, N. A. AS TRUSTEE (BAYVIEW) BY ITS ATTORNEY-IN-FACT BAYVIEW LOAN SERVICING, LLC**
4425 Ponce de Leon Blvd., Coral Gables, FL 33146

By: _____
ROBERT G. HALL, Vice-President

[106] ECF No. 21 at 20–21, ¶ 95.
[107] *Countrywide Home Loans, Inc. v. Cowin (In re Cowin)*, 492 B.R. 858, 888 (Bankr. S.D. Tex. 2013) (citing *Hill v. U.S. Bank, N.A. (In re Perry)*, 2013 Bankr. LEXIS 534, at *8 (Bankr. S.D. Tex. Feb. 8, 2013) (collecting cases)).
[108] *Reinagel*, 735 F.3d at 228 n.27.
[109] ECF No. 21 at 10, ¶ 43.
[110] ECF No. 21-7.

assignee on the second assignment.[111] The third assignment designates Bayview Loan Servicing, LLC, as the assignee and the signature block reflects:[112] Plaintiffs did not plead that Robert G. Hall, the signatory, lacked authority to act on behalf of Defendant or that Defendant lacked authority to act on behalf of Wachovia Bank, N.A. and thus, Plaintiffs' challenge to the validity of the third assignment fails.[113] Plaintiffs lack standing to challenge the third assignment because Texas Local Government Code section 192.007(a) does not affect the validity of the Deed of Trust and Plaintiffs did not plead that Defendant lacked authority to act on behalf of Wachovia Bank, N.A. as its attorney-in-fact. Defendant's Motion as to Plaintiffs' Count II regarding the assignments is granted.

Accordingly, Plaintiffs' Count II is dismissed with prejudice. The Court will not grant Plaintiffs leave to re-plead Count II under FRCP 15(a) because such an amendment would be futile where Count II also fails on *res judicata* grounds as explained below. Finally, Defendant's Motion to Dismiss does not question Plaintiffs' standing to challenge the validity of Defendant's lien based on the missing legal description in the Deed of Trust.[114] Nevertheless, that portion of Plaintiffs' Count II will also be dismissed on *res judicata* grounds as discussed more fully infra.

b. Whether Plaintiffs' claims are barred by judicial estoppel

Defendant argues that Plaintiffs are judicially estopped from challenging the validity of Defendant's lien in this case because they consistently acknowledged the validity of Defendant's lien in the 2011 Case.[115] Judicial estoppel may be properly raised in a motion to dismiss under FRCP 12(b)(6) where its application is warranted on the face of the pleadings and in judicially

[111] ECF No. 21-5.
[112] ECF No. 21-7.
[113] *See Reinagel*, 735 F.3d at 226 (finding that the plaintiffs' challenge to the validity of the assignment failed on its own terms because the plaintiffs did not allege that the signatory misrepresented the scope of her authority in executing the assignment as attorney in fact).
[114] See ECF No. 34 at 17–18.
[115] ECF No. 34 at 15.

noticed facts.[116] The doctrine is intended to "prevent[] internal inconsistency, preclude[] litigants from 'playing fast and loose' with the courts, and prohibit[] parties from deliberately changing positions based upon the exigencies of the moment."[117] In evaluating whether judicial estoppel should apply, courts in the Fifth Circuit consider whether: (i) the position of the party to be estopped is clearly inconsistent with its previous one; (ii) the party to be estopped convinced the court to accept that previous position; and (iii) the party to be estopped acted inadvertently.[118] This Court adds a fourth factor to its analysis and also considers (iv) whether Plaintiffs would derive an unfair advantage or impose an unfair detriment on Defendant if not estopped.[119]

i. Plaintiffs' position is clearly inconsistent with their previous one

The first judicial estoppel factor considers whether Plaintiffs' contention that Defendant's lien is invalid is contrary to Plaintiffs' position in the 2011 Case.[120] To find that Plaintiffs' position is inconsistent, Plaintiffs' change of position must be clear and express and not merely implied.[121] Plaintiffs' Complaint pled that Plaintiffs and Defendant executed a Modification Agreement before the 2011 Case, restructuring the Note[122] and Plaintiffs paid Defendant $1,197.00[123] in on-

[116] *U.S. ex rel. Long v. GSDMIdea City, L.L.C.*, 798 F.3d 265, 274–75, 274 n.7 (5th Cir. 2015). *See also Hall*, 305 F. App'x. at 227–28 (unpublished) ("If, based on the facts pleaded and judicially noticed, a successful affirmative defense appears, then dismissal under Rule 12(b)(6) is proper.") (citing *Kansa Reinsurance Co., Ltd.*, 20 F.3d at 1366); *Johnson v. Deutsche Bank Nat. Trust Co.*, 2013 WL 3810715, at *8 (N.D. Tex. July 23, 2013) ("[B]ecause the elements of judicial estoppel appear on the face of Plaintiff's complaint and in court filings that are subject to judicial notice, this affirmative defense may be properly considered for purposes of Defendants' motion to dismiss."); *Abreu v. Zale Corp.*, 2013 WL 1949845, at *1 (N.D. Tex. May 13, 2013) (considering judicial estoppel in the context of a motion for judgment on the pleadings under FRCP 12(c)).

[117] *Ergo Science, Inc. v. Martin*, 73 F.3d 595, 598 (5th Cir. 1996) (citing *United States v. McCaskey*, 9 F.3d 368, 378 (5th Cir. 1993)).

[118] *Love v. Tyson Foods, Inc.*, 677 F.3d 258, 261 (5th Cir. 2012) (quoting *Reed v. City of Arlington*, 650 F.3d 571, 573–74 (5th Cir. 2011) (en banc)).

[119] *New Hampshire v. Maine*, 532 U.S. 742, 750–51 (2001); Hollie *v. Bank of N.Y. Mellon (In re Hollie)*, 622 B.R. 221, 234 (Bankr. S.D. Tex. 2020) (citing *Hall v. GE Plastic Pac. PTE, Ltd.*, 327 F.3d 391, 396–400 (5th Cir. 2003)).

[120] *GE Plastic Pac. PTE, Ltd.*, 327 F.3d at 397 ("[A] party cannot advance one argument and then, for convenience or gamesmanship after that argument has served its purpose, advance a different and inconsistent argument.").

[121] *Wells Fargo Bank, N.A. v. Titus Chinedu Oparaji (In re Titus Chinedu Oparaji)*, 698 F.3d 231, 237 (5th Cir. 2012) (quoting *In re Condere Corp.*, 226 F.3d 642, 2000 WL 1029098, at *3 (5th Cir. 2000)).

[122] ECF No. 21 at 10, ¶ 38.

[123] Although Plaintiffs refer to the on-going mortgage payment in the amount of $1,197.40, the actual amount proposed in the confirmed plan was $1,197.00.

going mortgage payments under the 2011 Plan and thereafter according to this Court's Deem Current Order.[124] Those allegations show that Plaintiffs treated the lien as valid both before and during the 2011 Case.

Importantly, in the Agreed Order in the 2011 Case, this Court noted that Defendant and Plaintiffs, through their attorney, "reached an agreement whereby the automatic stay of 11 U.S.C. § 362 should be continued in effect" and stated:

> . . . the Debtors shall amend their Chapter 13 plan to provide for payment to the Chapter 13 Trustee through the Amended Plan of all future post-petition payments due Movant pursuant to that certain Promissory Note dated NOVEMBER 9, 2001 in the original principal sum of $68,000.00 executed by Debtors, bearing interest and being payable as therein set out and that certain Modification Agreement executed on or about JANUARY 25, 2010, being secured by the Deed of Trust and Security Agreement of even date therewith, filed in the Official Public Records of Real Property of HIDALGO County, Texas, and creating a valid, first and prior lien on improved real property in HIDALGO County, Texas, being further described as follows:
>
> > LOT SEVEN (7), DELLINGER SUBDIVISION, AN ADDITION TO THE CITY OF MERCEDES, HIDALGO COUNTY, TEXAS, AS PER MAP OR PLAT THEREOF RECORDED IN VOLUME 22, PAGE 39 MAP RECORDS, HIDALGO COUNTY TEXAS AND PROPERTY MORE COMMONLY KNOWN AS 3085 WEST EXPRESSWAY 83, MERCEDES, TEXAS 78596 ("PROPERTY").[125]

The signature of Plaintiffs' counsel, Raul E. Mora, affixed at the bottom of the Agreed Order approving and certifying compliance with Federal Rule of Bankruptcy Procedure 4001, represents Plaintiffs' acceptance of the validity of Defendant's lien in the 2011 Case.[126] Additionally,

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[124] ECF No. 21 at 12–14, ¶¶ 54, 56–57, 60, 64.

[125] 11-70475, ECF No. 91. Defendant requested that this Court take judicial notice of all docket entries in Case No. 11-70475 referenced in Defendant's Motion to Dismiss. ECF No. 34 at 5 n.2. Plaintiffs did not object. ECF No. 37. Taking judicial notice of matters of public record is proper in deciding a 12(b)(6) motion. *Norris v. Hearst Trust*, 500 F.3d 454, 461 n.9 (5th Cir. 2007). The docket entries in Case No. 11-70475 are "not subject to reasonable dispute because [they] can be accurately and readily determined from sources whose accuracy cannot reasonably be questioned." FED. R. EVID. 201(b)(2). Therefore, this Court takes judicial notice of all docket entries in Case No. 11-70475.

[126] *In re Hollie*, 622 B.R. at 235 (finding that the first factor of judicial estoppel was satisfied because the plaintiff had previously entered into an agreed judgment avoiding a completed foreclosure and reinstating the plaintiff's ownership in the property, indicating the plaintiff's acceptance of the validity of the loan).

Plaintiffs pled that after receiving their discharge on September 13, 2018, they continued making payments directly to Defendant until November 2018 when Plaintiffs "grew terribly frustrated with Defendant's practices post-discharge."[127] Thus, even after receiving a discharge in the 2011 Case, Plaintiffs continued to treat Defendant's lien as valid.

Accordingly, the first factor is satisfied.

ii. Plaintiffs convinced this Court to accept their previous position

The second judicial estoppel factor considers whether Plaintiffs convinced the court to accept its prior inconsistent position.[128] Referred to as the "prior success" or "judicial acceptance" factor, this requirement seeks to "minimize the danger of a party contradicting a court's determination based on the party's prior position and, thus, mitigate the corresponding threat to judicial integrity."[129] Judicial acceptance does not mean that the party to be estopped was successful on the merits; rather, it merely means that the party made the argument "with the explicit intent to induce the district court's reliance[,]"[130] and the court accepted or relied on the party's position in making a determination.[131] Courts exercise great caution in applying judicial estoppel "because the doctrine precludes a contradictory position without examining the truth of either statement."[132] This requires that the party seeking judicial estoppel "affirmatively show, by competent evidence or inescapable inference, that the prior court adopted or relied upon the previous inconsistent assertion."[133]

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[127] ECF No. 21 at 4, 15–16, ¶¶ 5, 70–71.
[128] *New Hampshire*, 532 U.S. at 749–50.
[129] *GE Plastic Pac. PTE, Ltd.*, 327 F.3d at 398 (cleaned up) (quoting *Brown Mfg. v. Mims (In re Coastal Plains, Inc.)*, 179 F.3d 197, 206 (5th Cir. 1999)).
[130] *Id.* (quoting *Hidden Oaks v. City of Austin*, 138 F.3d 1036, 1047 (5th Cir. 1998)).
[131] *Id.* (quoting *Ahrens v. Perot Sys. Corp.*, 205 F.3d 831, 836 (5th Cir. 2000)).
[132] *Perry v. Blum*, 629 F.2d 1, 11 (1st Cir. 2010) (quoting *Teledyne Indus., Inc. v. NLRB*, 911 F.2d 1214, 1218 (6th Cir. 1990)).
[133] *Id.* at 11–12 (first citing *United Steelworkers of Am. v. Ret. Income Plan for Hourly-Rated Emps. Of ASARCO, Inc.*, 512 F.3d 555, 563–64 (9th Cir. 2008); then citing *United States v. Levasseur*, 846 F.2d 786, 794 (1st Cir. 1988)). *See also Andrade v. Countrywide KB Home Loans*, 2015 U.S. Dist. LEXIS 116967, *21 (N.D. Tex. July 13, 2015) ("As

Entry of an agreed order that accepts a party's position generally satisfies the judicial acceptance factor.[134] This Court's Agreed Order in the 2011 Case stated, "it appearing that due notice of said Motion having been properly given by the Court, having considered said Motion and the agreement of counsel, is of the opinion that the following Agreed Order should be entered."[135] This Court accepted Plaintiffs' prior inconsistent position that the lien was valid when it entered the Agreed Order. Additionally, this Court's confirmation and approval of the modification to Plaintiffs' 2011 Plan constitutes acceptance.[136] Plaintiffs scheduled Defendant as a creditor holding a secured, undisputed claim[137] and provisioned for arrearage and on-going mortgage payments to Defendant in their 2011 Plan,[138] demonstrating that Plaintiffs accepted Defendant's lien as valid. This Court relied on that representation when it confirmed the 2011 Plan and approved the later modification.

Accordingly, the second factor of judicial estoppel is satisfied.

iii. Plaintiffs acted inadvertently

This factor asks whether Plaintiffs acted inadvertently in failing to assert their claim that Defendant's lien was invalid in the 2011 Case. In bankruptcy, "the debtor's failure to satisfy its statutory disclosure duty is 'inadvertent' only when, in general, the debtor either lacks knowledge

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with any affirmative defense, '[t]he burden to prove judicial estoppel is on the party invoking the doctrine.'") (quoting *Thompson v. Sanderson Farms, Inc.*, 2006 U.S. Dist. LEXIS 48409, at *8 (S.D. Miss. May 31, 2006)).

[134] *See*, *In re Hollie*, 622 B.R. at 235 (finding that "[e]ntry of a judgment that agrees with a litigant's position is undoubtedly the court's acceptance of a litigant's position."); *In re Save Our Springs (S.O.S.) Alliance, Inc.*, 393 B.R. 452, 458–61 (Bankr. W.D. Tex. 2008) (finding that the agreed order submitted by the debtor and its creditor for approval by the court, which indicated that the debtor was a small business, was one of several pieces of evidence indicating that the court previously accepted the debtor's position that it was a small business); *Fill It Up, LLC v. MS LZ Delta, LLC*, 342 F. Supp. 3d 707, 715–16 (N.D. Miss. 2018) (finding that the judicial acceptance prong was met because the debtor was granted an automatic stay in its bankruptcy proceedings and because the bankruptcy court subsequently entered an agreed order abandoning certain bankruptcy estate property).

[135] 11-70475, ECF No. 91.

[136] *See In re Rankin*, 141 B.R. 315, 322 (Bankr. W.D. Tex. 1992) (finding that judicial estoppel applied to the debtor's inconsistent position because the court previously accepted the debtor's prior position and confirmed the debtor's plan based on the fact that the creditor and another party withdrew their objections to the plan).

[137] 11-70475, ECF No. 1

[138] ECF No. 21 at 12–13, ¶¶ 53, 60.

of the undisclosed claims or has no motive for their concealment."[139] To lack knowledge of an undisclosed claim, Plaintiffs must have been unaware of the facts giving rise to their claim during the pendency of their 2011 Case.[140]

Here, Plaintiffs maintain that they failed to challenge the validity of Defendant's lien in the 2011 Case because they were unaware of the allegedly deficient assignments due to Defendant's failure to disclose those assignments in the prior case.[141] However, Plaintiffs' Complaint also states that the third deficient assignment was recorded in Hidalgo County on August 1, 2011, [142] the same day Plaintiffs filed the 2011 Case, and thus was discoverable in the public records during the pendency of that case.[143] Additionally, Plaintiffs had access to the Deed of Trust with the missing legal description as far back as November 9, 2001. Because the facts on which Plaintiffs' Counts I and II are based were available to Plaintiffs from the beginning, Plaintiffs did not lack knowledge of their claims.

Courts also consider whether the offending party had any motive to conceal the claim. In the Fifth Circuit, "the motivation sub-element is almost always met if a debtor fails to disclose a claim or possible claim to the bankruptcy court. Motivation in this context is self-evident because of potential financial benefit resulting from the nondisclosure."[144] The pertinent inquiry is whether Plaintiffs would reap a windfall if they are able to recover on the undisclosed claim without having disclosed it to their creditors in their 2011 Case.[145] That result "would permit debtors to 'conceal

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[139] *Id.* at 210.
[140] *See Jethroe v. Omnova Solutions, Inc.*, 412 F.3d 598, 600 (5th Cir. 2005) ("According to *Browning*, to claim that her failure to disclose was inadvertent [the debtor] must show not that she was unaware that she had a duty to disclose her claims but that, at the time she filed her bankruptcy petition, she was unaware of the facts giving rise to them.") (citing *In re Coastal Plains, Inc.*, 179 F.3d at 211–12).
[141] ECF No. 37 at 11.
[142] ECF No. 21 at 10, ¶ 40.
[143] 11-70475, ECF No. 1.
[144] *Love*, 677 F.3d at 262 (cleaned up) (quoting *Thompson v. Sanderson Farms, Inc.*, 2006 U.S. Dist. LEXIS 48409, at *12–13 (S.D. Miss. May 31, 2006)).
[145] *Superior Crewboats, Inc. v. P & I Underwriters (In re Superior Crewboats, Inc.)*, 374 F.3d 330, 336 (5th Cir.

their claims; get rid of [their] creditors on the cheap, and start over with a bundle of rights.'"[146] The debtor's intent at the time of the non-disclosure controls the Court's analysis of this sub-element.[147]

"[A] debtor's motive to conceal is presumed as a matter of law—because of the structure of the bankruptcy process, a debtor that fails to disclose a claim during the bankruptcy, but later pursues it after discharge or confirmation, always has the potential to gain a windfall."[148] Based on Plaintiffs' Complaint and judicially noticed facts, Plaintiffs' intent at the time of the non-disclosure in the 2011 Case was to treat Defendant's lien as if it was valid and continue to make payments thereon. Frustrated by "[Defendant]'s practices post-discharge," however, Plaintiffs stopped making payments on the debt only two months after receiving a discharge.[149] Only now do Plaintiffs assert that Defendant's lien is invalid. But Plaintiffs' motivation after the bankruptcy case was closed or discharged is irrelevant; their motivation at the time of the non-disclosure is all this Court can consider. [150]

Additionally, Plaintiffs' 2011 Plan proposed to pay unsecured creditors 20% pro rata but was subsequently modified to pay unsecured creditors at 100%.[151] That plan modification was approved.[152] The chapter 13 trustee's Final Report and Account reflects that Plaintiffs' unsecured claims were paid in full.[153] Plaintiffs would not reap a windfall if they were able to recover on the undisclosed claim without disclosing that claim to the creditors in their 2011 Case because the

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2004).
[146] *In re Superior Crewboats*, 374 F.3d at 336 (quoting *Payless Wholesale Distribs., Inc. v. Alberto Culver, Inc.*, 989 F.2d 570, 571 (1st Cir. 1993)).
[147] *Love*, 677 F.3d at 263 (quoting *Robinson v. Tyson Foods, Inc.*, 595 F.3d 1269, 1276 (11th Cir. 2010)).
[148] *ASARCO, LLC v. Mont. Res., Inc.*, 514 B.R. 168, 195–96 (S.D. Tex. 2013) (citing *Love*, 677 F.3d at 262).
[149] ECF No. 21 at 15–16, ¶ 71.
[150] *Allen v. C & H Distribs., L.L.C.*, 813 F.3d 566, 574 (5th Cir. 2015).
[151] 11-70475, ECF No. 184-1 at 15, ¶ 10.
[152] 11-70475, ECF No. 186.
[153] 11-70475, ECF No. 225.

2011 Plan as modified was a 100% plan. Consequently, the presumption that Plaintiffs had a motive to conceal is rebutted by Plaintiffs' Complaint and judicially noticed facts. Application of judicial estoppel is not appropriate where a party acted inadvertently either because it lacked knowledge of the undisclosed claim or had no motive for concealment.[154] Plaintiffs acted inadvertently because they had no motive to conceal the claim.

Accordingly, the third factor is not satisfied.

iv. Plaintiffs would derive an unfair advantage if not estopped

The Court considers whether Plaintiffs would receive an unfair advantage or impose an unfair detriment on Defendant if not estopped.[155] As discussed above, Plaintiffs' Complaint reflects that they acknowledged the validity of the lien throughout their 2011 Case when doing so benefitted them from plan confirmation to discharge. Plaintiffs' Complaint also reflects that they quit making their mortgage payments only after they became frustrated with Defendant's post-discharge behavior and disavowed the lien's validity for the first time in their Objection in the instant case. To permit Plaintiffs to acknowledge the validity of Defendant's lien when it is in their interest and now disavow that lien because their interests have changed would confer an unfair advantage on Plaintiffs.[156]

The fourth factor is satisfied. Nevertheless, despite finding that three of the four factors of judicial estoppel are met, the Court finds that Plaintiffs acted inadvertently in the 2011 Case and thus, judicial estoppel is not appropriate.

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[154] *United States ex rel. Long v. GSDMIdea City, L.L.C.*, 798 F.3d 265, 272 (5th Cir. 2015) ("To be sure, if a debtor's failing to disclose was inadvertent, judicial estoppel is inappropriate . . . .").
[155] *New Hampshire*, 532 U.S. at 751.
[156] *See Knigge v. SunTrust Mortg., Inc. (In re Knigge)*, 479 B.R. 500, 508 (8th Cir. B.A.P. 2012) (estopping the debtors from arguing that the mortgage company lacked standing to enforce a promissory note and deed of trust after the debtors recognized the lien as valid in their previous bankruptcy case, noting "[w]e will not permit the Debtors to acknowledge [the mortgagee's] lien when it was in their interest, and then change their position to contest [the mortgagee's] position when that would provide them with an advantage in their adversary proceeding.").

Accordingly, Defendant's request for dismissal on the grounds of judicial estoppel is denied.

c. Whether Plaintiffs' claims are barred by *res judicata*

Defendant asserts that Plaintiffs' Counts I and II, relating to the validity of the lien and seeking avoidance of the loan and lien, may not be asserted in this adversary proceeding because they are barred by *res judicata* and the claims should accordingly be dismissed.[157] The preclusive effect of a judgment is defined by claim preclusion and issue preclusion, which are collectively referred to as *res judicata*.[158] *Res judicata* applies with equal force in the context of bankruptcy proceedings.[159] The doctrine of *res judicata* bars litigation of a claim previously litigated or one that could or should have been raised in a prior suit if: (1) the parties are identical in both actions; (2) a court of competent jurisdiction rendered the prior judgement; (3) there was a final adjudication on the merits; and (4) both cases involve the same cause of action.[160]

Defendant argues that "Plaintiffs' claims are barred by *res judicata* based on this Court's entry of the Agreed Order Relative to the Automatic Stay of 11 U.S.C. § 362 in [case number 11-70475]."[161] Defendant contends that: (1) the parties in this proceeding are identical to those in Plaintiffs' prior chapter 13 case; (2) this Court issued the prior Agreed Order[162] and is a court of competent jurisdiction over the claims allowance process in the prior case; (3) the Agreed Order was final and appealable even though Plaintiffs failed to appeal; and (4) both cases involve the same causes of action—Defendant's proof of claim against Plaintiffs[163] and the validity of

[157] ECF No. 34 at 11.
[158] *Taylor v. Sturgell*, 553 U.S. 880, 892 (2008).
[159] *In re Paige*, 610 F.3d 865, 870 n.1 (5th Cir. 2010) (citing *In re Baudoin*, 981 F.2d 736, 740 (5th Cir. 1993) ("This Court has [long] recognized the important interest in the finality of judgments in a bankruptcy case.")).
[160] *In re Shank*, 569 B.R. 238, 257 (Bankr. S.D. Tex. 2017).
[161] ECF No. 34 at 13.
[162] 11-70475, ECF No. 91.
[163] ECF No. 34 at 13–14.

Defendant's lien on the Property[164]—which have been resolved by this Court.[165] Defendant further argues that even if Plaintiffs did not challenge the validity of Defendant's lien in the 2011 Case, they should have, and where a plaintiff failed to raise a claim that could or should have been raised in an earlier suit, that claim is barred by *res judicata*.[166]

Plaintiffs respond that "generally a *res judicata* contention cannot be brought in a motion to dismiss; it must be pleaded as an affirmative defense."[167] Plaintiffs insist that the validity of Defendant's lien was not litigated because (1) there was no litigated objection to Defendant's claim in the 2011 Case, and therefore, the voidness of the lien, the invalidity of the assignments, and Defendant's status as a lienholder was not questioned; and (2) to challenge the validity of Defendant's lien, Federal Rule of Bankruptcy Procedure 7001(2) requires Plaintiffs to bring an adversary proceeding, which they did not do previously.[168] Plaintiffs also contend that three deficient assignments form the basis of Plaintiffs' claim that Defendant's lien is void and those deficient assignments were not presented in the 2011 Case.[169] Only in the current bankruptcy case, Plaintiffs continue, did Defendant attach one of the deficient assignments to its proof of claim.[170]

Lastly, Plaintiffs argue that because Defendant's lien is void, not merely voidable, *res judicata* cannot cutoff Plaintiffs' constitutional rights under section 50(c) of the Texas Constitution to a determination of quiet title.[171] In support, Plaintiffs cite *Jackson*, which says, "[f]aced with changing law, courts hearing questions of constitutional right cannot be limited by res judicata. If

[164] ECF No. 38 at 2.
[165] ECF No. 34 at 13–14.
[166] ECF No. 38 at 4 (citing *Petro-Hunt, L.L.C. v. U.S.*, 365 F.3d 385, 395 (5th Cir. 2004)).
[167] ECF No. 37 at 10 (citing *Hall v. Hodgkins*, 305 F. App'x 224, 227 (5th Cir. 2008)).
[168] *Id.* at 11–12.
[169] *Id.* at 12–13.
[170] *Id.*
[171] ECF No. 37 at 11; *see Wood v. HSBC Bank USA, N.A.*, 505 S.W.3d 525, 550 (Tex. 2016) (holding that no statute of limitations applies to cut off a homeowner's right to quiet title to real property encumbered by an invalid lien under article 16, section 50(c) of the Texas Constitution).

they were, the Constitution would be applied differently in different locations."[172] This Court disagrees with Plaintiffs. The Court in *Jackson* is not referring to the Texas Constitution, but rather to the United States Constitution. Because Plaintiffs are alleging that Defendant's lien is void under the Texas Constitution, Texas law controls. As this Court acknowledged in *Hollie*, "Texas courts have recognized that claims based on violations of the home equity provisions of the Texas Constitution may be barred by *res judicata*."[173] Accordingly, if Plaintiffs should have challenged the validity of Defendant's lien in the 2011 Case, it may be barred by *res judicata* under Texas law.

i. This Court may consider both Plaintiffs' Complaint and any judicially noticed facts for purposes of *res judicata*

Generally, *res judicata* should not be raised in a motion to dismiss and is reserved for summary judgment or trial.[174] Two exceptions apply. The first, permitting a Court to treat a motion to dismiss based on *res judicata* as a motion for summary judgment, is not applicable in this case. Relevant here and forming the basis of the parties' disagreement is the exception that a finding of *res judicata* can be made at the motion to dismiss stage, if a successful affirmative defense of *res judicata* appears from the facts pled.[175] Based on the case law cited below, the parties disagree as to whether *res judicata* must appear on the face of the complaint alone or whether judicially noticed facts may also be considered.

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[172] *Jackson v. De Soto Parish Sch. Bd.*, 585 F.2d 726, 729 (5th Cir. 1978) (quoting *Parnell v. Rapides Parish Sch. Bd.*, 563 F.2d 180, 185 (5th Cir. 1977)).
[173] *Hollie v. Bank of N.Y. Mellon (In re Hollie)*, 622 B.R. 221, 230 (Bankr. S.D. Tex. 2020).
[174] *See Johnson-Williams v. CitiMortgage, Inc.*, 2018 U.S. Dist. LEXIS 33504, at *19 (N.D. Tex. Jan. 31, 2018) (citing *Am. Realty Trust, Inc. v. Hamilton Lane Advisors, Inc.*, 115 F. App'x 662, 664 n.1 (5th Cir. 2004)); *see also e.g.*, *Moch v. East Baton Rouge Parish School Bd.*, 548 f.2d 594, 596 n.3 (5th Cir. 1977) ("Generally, a party cannot base a 12(b)(6) motion on res judicata."); *Amoco Prod. Co.*, 794 f.2d 967, 970 (5th Cir. 1986) (noting that FRCP 12(b)(6) only applies to affirmative defenses that appear on the face of the plaintiffs' complaint).
[175] *Limon v. Berryco Barge Lines, L.L.C.*, 779 F. Supp. 2d 577, 581–83 (S.D. Tex. 2011) (noting that two exceptions to the bar on *res judicata* in a motion to dismiss are recognized in the Fifth Circuit).

Citing to the Fifth Circuit's *Hall* and *Kansa* opinions, Defendant maintains that *res judicata* is appropriate at the motion to dismiss stage if it appears on the face of the complaint and any judicially noticed facts.[176] Defendant asks this Court to take judicial notice of the Agreed Order in Plaintiffs' previous chapter 13 bankruptcy, which states in part that the promissory note secured by a deed of trust and security agreement created a valid, first and prior lien on the Property.[177] Nevertheless, Defendant says, even if judicially noticed facts cannot be considered, *res judicata* appears on the face of Plaintiffs' Complaint.[178] In *Hall*, the Fifth Circuit notes that "[i]n ruling on a FRCP 12(b)(6) motion to dismiss, the district court cannot look beyond the pleadings," but that "[i]n addition to facts alleged in the pleadings, however, the district court 'may also consider matters of which [it] may take judicial notice.'"[179] Citing its earlier decision, *Kansa*, the Court concluded that "[i]f, based on the facts pleaded *and judicially noticed*, a successful affirmative defense appears, then dismissal under FRCP 12(b)(6) is proper."[180]

Plaintiffs, on the other hand, citing to *Grynberg* and *Pike*, insist that *res judicata* must appear on the face of the pleadings alone and that it does not appear solely from the facts pled in their Complaint.[181] In *Grynberg*, the Southern District of Texas said, "unless the complaint itself sets forth the facts necessary to determine that *res judicata* precludes adjudication, summary judgment is the proper standard for determining whether a claim should be dismissed on *res judicata*."[182] And in *Pike*, the district court in Louisiana explained that although judicial notice is

[176] ECF No. 34 at 11.
[177] *See* ECF No. 34 at 1 n.1 (citing 11-70475, ECF No. 91).
[178] ECF No. 38 at 1–2.
[179] 305 F. App'x 224, 227 (2008) (citing *Lovelace*, 78 F.3d 1015, 1017–18 (5th Cir. 1996)).
[180] *Id.* at 227–28 (emphasis added) (citing *Kansa Reinsurance Co., Ltd. v. Cong. Mortg. Corp. of Tex.*, 20 F.3d 1362, 1366 (5th Cir. 1994)).
[181] ECF No. 37 at 10.
[182] *Grynberg v. BP P.L.C.*, 855 F. Supp. 2d 625, 648 (S.D. Tex. 2012) *aff'd*, 527 F. App'x 278 (5th Cir. 2013)).

appropriate on a motion to dismiss, it must nevertheless be "readily apparent on the face of [the] pleadings that *res judicata* should apply."[183]

Both parties overlook a recent Fifth Circuit decision that in no uncertain terms states, "dismissal under FRCP 12(b)(6) is appropriate if the res judicata bar is apparent from the pleadings and judicially noticed facts."[184] *Basic Capital Management* is binding on this Court and more recent than *Grynberg* and *Pike*. Therefore, this Court may look to both Plaintiffs' Complaint and judicially noticed facts. This Court will consider the Complaint first.

ii. A successful *res judicata* defense appears of the face of Plaintiffs' Complaint

Defendant is correct that facts to satisfy the first three elements of *res judicata*—the parties, a court of competent jurisdiction, and final adjudication on the merits—appear on the face of Plaintiffs' Complaint. Plaintiffs pled that Defendant filed a proof of claim in Plaintiffs' 2011 Case and that the Agreed Order was entered by this Court in presiding over that bankruptcy case.[185] The Agreed Order, which Plaintiffs' Complaint indicates granted Defendant's Motion to Lift Stay, was a final order and is entitled to full *res judicata* effect.[186]

Whether the fourth element—the same cause of action in both cases—appears on the face of Plaintiffs' Complaint requires closer scrutiny. In assessing the fourth element, the Fifth Circuit employs the transactional test, which asks whether the prior case and the current case are based on the same nucleus of operative facts.[187] Courts must question "whether the facts are related in time,

[183] *Pike v. Off. of Alcohol & Tobacco Control of the Louisiana Dep't of Revenue*, 157 F. Supp. 3d 523, 531 (M.D. La. 2015).
[184] *Basic Capital Mgmt. v. Dynex Capital, Inc.*, 976 F.3d 585, 591 (5th Cir. 2020) (quoting *Kahn v. Ripley*, 772 F. App'x 141, 142 (5th Cir. 2019)).
[185] *See* ECF No. 21 at 12, ¶¶ 52–54, 57.
[186] *See, e.g.*, *Chunn v. Chunn (In re Chunn)*, 106 F.3d 1239, 1241 (5th Cir. 1997) ("We . . . conclude that an order granting relief from an automatic stay is a final and appealable order."); *In re Hollie*, 622 B.R. at 231 ("Courts routinely recognize that an agreed judgment . . . is final and entitled to full *res judicata* effect.").
[187] *United States v. Davenport*, 484 F.3d 321, 326 (5th Cir. 2007).

space, origin, or motivation."[188] Here, the face of Plaintiffs' Complaint shows that Defendant's proofs of claim in both the 2011 Case and the instant bankruptcy case were based on the same mortgage loan[189] and that those proofs of claim and the amounts owed to Defendant are central in both cases.[190] The Complaint also specifies that Plaintiffs were motivated to file the 2011 Case and the present case for the same reason: to prevent foreclosure. Plaintiffs' Complaint states, "[t]he [Plaintiffs] filed the present bankruptcy case to stop [Defendant's] foreclosure[,]"[191] and details a series of prior bankruptcy cases filed by Plaintiffs starting in 2002, to "preserve the properties at issue and resolve all accounting issues."[192]

The Court concludes that the 2011 Case and the instant case are based on the same nucleus of operative facts because those facts are related in time, space, origin, and motivation. Finding that the four elements of *res judicata* are apparent on the face of the pleadings, this Court now considers whether Plaintiffs should have challenged the validity of Defendant's lien in the 2011 Case.[193]

Plaintiffs' Counts I and II challenge the validity of Defendant's lien on different bases. Count I alleges that Defendant's lien on Plaintiffs' Property is a lien on a homestead created by a commercial loan in violation of section 50(a) of the Texas Constitution.[194] In support, Plaintiffs allege that: (1) InterBay's loan documents included statements that the loan was a commercial one; (2) Mr. Bocanegra, an agent of the original lender, InterBay, knew Plaintiffs lived at the property;

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[188] *Jackson v. Novastar Mortg., Inc.*, 2014 U.S. Dist. LEXIS 189382, at *10 (S.D. Tex. Feb. 6, 2014) (quoting *Test Masters*, 428 F.3d at 571).
[189] ECF No. 21 at 4–5, 10–12, ¶¶ 5, 7, 22, 44–57.
[190] *Id.* at 10–13, ¶¶ 44–57.
[191] *Id.* at 4, 17, ¶¶ 5, 79.
[192] *Id.* at 4, ¶ 4.
[193] *See D-1 Enters., Inc. v. Commercial State Bank*, 864 F.2d 36, 38 (5th Cir. 1989) ("Essential to the application of the doctrine of *res judicata* is the principle that the previously unlitigated claim to be precluded could and should have been brought in the earlier litigation.") (citing *Southmark Props. v. Charles House Corp.*, 742 F.2d 862, 871 (5th Cir. 1984)).
[194] ECF No. 21 at 19, ¶ 88.

(3) Plaintiffs' Application was titled "Uniform Residential Loan Application"; and (4) that Application indicated that the Property was Plaintiffs' primary residence.[195] Count II alleges that Defendant's lien is invalid because the Deed of Trust does not contain a legal description and the three assignments purporting to make Defendant the legal holder of the Note and Deed of Trust were defective.[196]

Plaintiffs claim that they couldn't have challenged the lien's validity in the 2011 Case because the deficient assignments were not previously produced by Defendant. However, per Plaintiffs' Complaint, the third assignment was recorded in Hidalgo County on August 1, 2011,[197] the same day Plaintiffs filed the 2011 Case, and approximately five months before Defendant's Motion to Lift Stay was filed and six months before this Court entered the Agreed Order resolving that motion.[198] Because the third assignment was public record at the time and could have been discovered, Plaintiffs' argument that the assignments were new facts discovered after January 27, 2012, when the Agreed Order was entered,[199] is without merit.. Similarly, the Deed of Trust was executed November 9, 2001,[200] making any of the discrepancies therein discoverable a decade before the 2011 Case.

Moreover, an analogous Texas state court case—*Belay*—applying the federal law of *res judicata*, illustrates why Plaintiffs should have challenged Defendant's lien in the 2011 Case. In *Belay*, shortly after receiving notice of judicial foreclosure on her home equity loan, a homeowner filed for bankruptcy.[201] The bankruptcy proceeding was dismissed and several months later, the

[195] *Id.* at 3–4, 7–8, ¶¶ 2, 21–25.
[196] *Id.* at 20–21, ¶¶ 92–96.
[197] *Id.* at 10, ¶ 40.
[198] *Id.* at 12–13, ¶ 57 (indicating that Community's Motion to Lift Stay was filed on December 21, 2011, and this Court entered the Agreed Order resolving that motion on January 27, 2012).
[199] ECF No. 37 at 12–13.
[200] ECF No. 21 at 7, ¶ 21.
[201] *Belay v. Wells Fargo Bank, N.A.*, 2020 Tex. App. LEXIS 5514, at *1 (Tex. App.—Amarillo Jul. 16, 2020, no pet.).

debtor filed a second bankruptcy petition. The lender filed a motion to lift the stay so that it could foreclose on the debtor's property. In that motion, the lender indicated that the debtor had 14 days to file a timely response to the motion, otherwise the motion could be granted without a hearing. The debtor filed her objection 19 days later, attaching an affidavit claiming that she did not sign or authorize the loan referenced in the lender's proof of claim and did not sign the deed of trust. The bankruptcy court granted the lender's motion on the basis that timely response was not filed and entered an order lifting the stay. The debtor did not appeal that order.

In the state district court, the lender filed a motion to reinstate the judicial foreclosure proceeding. In response, the debtor argued that the lender could not foreclose on the home equity loan because it was void under the section 50(a) of the Texas Constitution. The lender filed a motion for summary judgment asserting that the debtor's claim was barred by *res judicata* because she should have challenged the validity of the home equity loan in the bankruptcy court. Affirming the state district court, the appellate court, applying the federal law of *res judicata* found all four elements of the doctrine satisfied. The court further concluded that even though the validity of the lien was unlitigated in the bankruptcy court, it could and should have been because the lender's interest in the debtor's property was placed squarely before the bankruptcy court and determining whether a lender's lien is void goes directly to the issues to be determined in deciding on a motion to lift stay for purposes of foreclosure.

This case is strikingly similar to *Belay*. Plaintiffs' Complaint reveals that the mortgage and balance thereof were at issue in the 2011 Case because Defendant's Motion to Lift Stay represented that Plaintiffs' ongoing monthly mortgage payments were $1,197.40 and the Agreed Order resolving that motion, ordered Plaintiffs to continue paying $1,197.40 per month and not the increased

amount of $1,251.57 as detailed in Defendant's NPC filed the month prior.[202] Furthermore, just as the homeowner in *Belay* filed bankruptcy to halt foreclosure, Plaintiffs' Complaint acknowledges that Plaintiffs' 2011 Case was filed to "preserve the properties at issue."[203]

Although unlitigated in the 2011 Case, the validity of Defendant's lien was placed squarely at issue when Defendant filed its Motion to Lift Stay and Plaintiffs could and should have challenged the lien's validity then. Given Plaintiffs' factual allegations, a successful affirmative *res judicata* defense so plainly appears on the face of Plaintiffs' Complaint alone that Plaintiffs' Counts I and II cannot survive Defendant's FRCP 12(b)(6) challenge.

Accordingly, Defendant's Motion to Dismiss on *res judicata* grounds is granted. Plaintiffs' Counts I and II are dismissed with prejudice. Additionally, Plaintiffs' challenge to the validity of the lien based on the missing legal description in the Deed of Trust under Count II is dismissed with prejudice on these grounds as well.

2. Plaintiffs' Count III (violations of Federal Rule of Bankruptcy Procedure 3002.1)

Plaintiffs' Count III alleges that Defendant violated Federal Rule of Bankruptcy Procedure 3002.1(b) and (c). Plaintiffs allege that Defendant changed Plaintiffs' monthly mortgage payment three times—on September 1, 2013 to $1,276; on October 1, 2014 to $1,195; and on December 1, 2015 to $1,454—without filing the required Rule 3002.1(b) notice. Plaintiffs also allege that Defendant violated Rule 3002.1(c) by assessing "BK Fees, Legal Fees or Costs, Property Inspection Fees, and Title Costs," during the 2011 Case without filing the correct notice.[204] Defendant moves for dismissal of Count III, on the basis that (a) as a procedural rule, Rule 3002.1 does not create a private cause of action; (b) violations of Rule 3002.1 in a prior case cannot be brought in a

[202] ECF No. 21 at 10–11, ¶¶ 56–57.
[203] *Id.* at 4, ¶ 4.
[204] ECF No. 21 at 17–18, 22–23, ¶¶ 80–81, 99, 104.

subsequent unrelated adversarial proceeding; (c) punitive monetary sanctions are not permitted under Rule 3002.1(i)(2); and (d) in the alternative, Plaintiffs have not pled any harm by Defendant's alleged failures to comply with Rule 3002.1.[205] The Court will consider each in turn.

Rule 3002.1 applies to claims that are secured by a security interest in the debtor's principal residence and for which the plan provides that either the trustee or the debtor will make contractual installment payments.[206] Rule 3002.1(b)(1) requires the holder of a claim to file and serve on the debtor, debtor's counsel, and the trustee a notice of any change in the payment amount, including any change that results from an interest-rate or escrow-account adjustment, no later than 21 days before a payment in the new amount is due.[207] The Rule also provides the debtor an opportunity to object to such payment change by filing a motion to determine whether it is warranted.[208] "If no motion is filed by the day before the new amount is due, the change goes into effect, unless the court orders otherwise."[209]

Subsection (c) of the Rule requires a holder of a claim to serve a notice itemizing fees, expenses, and charges "(1) that were incurred in connection with the claim after the bankruptcy case was filed; and (2) that the holder asserts are recoverable against the debtor or against the debtor's principal residence."[210] If the holder of a claim does not comply with these provisions, a court may "(1) preclude the holder from presenting the omitted information, in any form, as evidence in any contested matter or adversary proceeding in the case, unless the court determines that the failure was substantially justified or is harmless; or (2) award other appropriate relief, including reasonable expenses and attorney's fees caused by the failure."[211]

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[205] ECF No. 34 at 19–20.
[206] FED. R. BANKR. P. 3002.1(a).
[207] *Id.* at 3002.1(b)(1).
[208] *Id.* at 3002.1(b)(2).
[209] *Id.*
[210] *Id.* at 3002.1(c).
[211] *Id.* at 3002.1(i).

a. Whether Rule 3002.1 creates an independent cause of action

Defendant's first argument is that Rule 3002.1 is nothing more than a procedural rule, which does not in itself create a freestanding cause of action that is otherwise unavailable under substantive law for recovery of damages for an injury.[212] Thus, Defendant concludes, "Plaintiffs are not entitled to use Rule 3002.1 as a basis for seeking recovery of actual damages, punitive damages, and/or sanctions."[213] In support, Defendant cites an unpublished letter to counsel—*In re Tollstrup*—from the District of Oregon bankruptcy court.[214] Plaintiffs counter that several courts, including this one, have already decided that Rule 3002.1 does create an independent cause of action.

The plain language of Rule 3002.1(i) provides that where "the holder of a claim fails to provide any information as required by subdivision (b), (c), or (g) of this rule, the court may, after notice and hearing . . . award other appropriate relief, including reasonable expenses and attorney's fees caused by the failure."[215] Rule 3002.1 lays out both the grounds of violation—failure to follow subdivision (b), (c), or (g)—and a remedy for such violations—appropriate relief.[216] Even the advisory committee notes recognize that a chapter 13 debtor who has made all plan payments and whose case has been closed may move to have the case reopened for the purpose of seeking sanctions under Rule 3002.1(i).[217]

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[212] ECF No. 34 at 21.
[213] ECF No. 34 at 21.
[214] ECF No. 34 at 20–21 (citing 2018 Bankr. LEXIS 767 (Bankr. D. Or. Mar. 16, 2018)). The court in *Tollstrup* says, "Counsel: I write to explain my separate ruling on Debtors' [*sic*] Request for Hearing re: Notice of Mortgage Payment Change Filed by Nationstar Mortgage LLC and Motion for Additional Relief1Link to the text of the note filed by debtor, Kenneth Ray Tollstrup. I will grant Tollstrup's motion but deny his request for punitive sanctions against Nationstar. He may separately move for an award of attorney fees and costs. This letter constitutes my findings of fact and conclusions of law." 2018 Bankr. LEXIS 767, at *1.
[215] FED. R. BANKR. P. 3002.1(i)(1).
[216] *Id.*
[217] FED. R. BANKR. P. 3002.1 advisory committee's note to 2011 adoption.

Nevertheless, this Court need not decide whether Rule 3002.1 creates an independent cause of action because Plaintiffs allege that Defendant violated Rule 3002.1(b) and (c) and subdivision (i)(2) permits this Court to award ". . . other appropriate relief, including reasonable expenses and attorney's fees. . ." for such violations.[218] In *Trevino*, this Court held that although the plaintiffs there could have utilized a Rule 3002.1(e) contested matter to object to the defendants' 3002.1(c) notice, plaintiffs could also raise the objection in an adversary proceeding and in fact, *must* file an adversary proceeding when seeking to recover money or property.[219] Here, Plaintiffs seek an array of sanctions, including the recovery of money for Defendant's alleged violations of the Rule. Thus, it was appropriate for Plaintiffs to bring their Rule 3002.1 violations in this adversary proceeding.

Tollstrup, a non-binding opinion cited by Defendant, is not inconsistent with permitting Plaintiffs in this case to set forth allegations of Rule 3002.1 violations in this adversary proceeding. In *Tollstrup*, the court found that the mortgagee violated Rule 3002.1(b) by providing inaccurate information in its Notice of Mortgage Payment Change and therefore, the mortgagee was subject to the sanctions described in Rule 3002.1(i). The portion of *Tollstrup* that Defendant relies on is merely the court's explanation as to why the debtor was not entitled to compensatory damages, an issue this Court discusses below.[220]

The debtor in *Tollstrup* sought several remedies, including evidence preclusion, attorney's fees and costs, and punitive damages.[221] The debtor additionally asked the court to find the correct amount of the future monthly payments, that the debtor was current on his mortgage payments, that the debtor owed no fees, costs, or charges to the mortgagee, and that the escrow was "in

[218] FED. R. BANKR. P. 3002.1(i)(2).
[219] *Trevino v. HSBC Mortg. Servs. (In re Trevino)*, 535 B.R. 110, 127 (Bankr. S.D. Tex. 2015) (citing FED. R. BANKR. P. 7001(1)).
[220] 2018 Bankr. LEXIS 767, at *9–11.
[221] *Id.* at *7–8.

balance with no shortage or excess due."[222] The court noted that due to a previous finding, most of the debtor's request were no longer relevant and thus, the court would focus solely on the request for attorney's fees and punitive damages.

In discussing which sanctions are appropriate under the Rule, the court said that Rule 3002.1 "is akin to a mandatory discovery or other disclosure requirement. It is not a substantive debtor-protection requirement analogous to the automatic stay or discharge injunction."[223] Citing to 28 U.S.C. § 2075,[224] the court concluded that because Rule 3002.1 is a procedural rule and procedural rules "cannot create independent causes of action that are unavailable under applicable substantive law[,]" the Rule does not create "a freestanding, substantive right to recover damages for an injury[,]" and thus, the debtor was not entitled to compensatory damages.[225] The court permitted the debtor to move forward with a request for costs and attorney's fees.[226]

Plaintiffs here, just as the debtor in *Tollstrup*, seek to impose sanctions against Defendant for allegedly violating Rule 3002.1(b) and (c). What sanctions this Court may impose under the Rule is a different question. It does not change the fact that *Tollstrup* recognizes that a debtor may allege a violation of the Rule and that a mortgagee may be sanctioned under Rule 3002.1(i) for such violations. Thus, this Court need not decide whether Rule 3002.1 creates a private federal cause of action. Based on the plain language of the Rule and this Court's decision in *Trevino*, Plaintiffs may set forth their Rule 3002.1 violation in an adversary proceeding, and more specifically in this Complaint.

Accordingly, Defendant's Motion to Dismiss Plaintiffs' Count III on this basis is denied.

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[222] *Id.*
[223] 2018 Bankr. LEXIS 767, at *9.
[224] 28 U.S.C. § 2075 provides: "The Supreme court shall have the power to prescribe by general rules, the forms of process, writs, pleadings, and motions, and the practice and procedure in cases under title 11. Such rules shall not abridge, enlarge, or modify any substantive right."
[225] 2018 Bankr. LEXIS 767, at *11–12.
[226] *Id.* at *14.

b. Plaintiffs' Count III for Rule 3002.1 violations committed in the 2011 Case is appropriate in this case

Defendant also argues that it is improper for Plaintiffs to seek damages for alleged violations of Rule 3002.1 occurring in the 2011 Case in a subsequent, unrelated adversary action.[227] In support, Defendant points to the plain language of the Rule itself: "the court may . . . preclude the holder from presenting the omitted information, in any form, as evidence in any contested matter or adversary proceeding *in the case*[,]" which does not indicate that relief may be sought in a case other than the bankruptcy case in which the violation occurred.[228] Defendant also points to the Advisory Committee Notes of Rule 3002.1, which states:

> If, after the chapter 13 debtor has completed payments under the plan and the case has been closed, the holder of a claim secured by the debtor's principal residence seeks to recover amounts that should have been but were not disclosed under this rule, *the debtor may move to have the case reopened in order to seek sanctions* against the holder of the claim under subdivision (i).[229]

Plaintiffs do not address this argument in their Response.[230]

While the advisory committee note makes clear that a debtor may move to reopen a case to seek sanctions under Rule 3002.1(i), nothing in the note prevents a debtor from bringing a Rule 3002.1 violation in a subsequent case. More importantly, this Court is unpersuaded that the plain language of Rule 3002.1 prevents a debtor from seeking "appropriate relief, including reasonable expenses and attorney's fees caused by the failure[,]" in a subsequent case.[231] The Rule expressly permits the court to preclude the claim holder from presenting omitted information in "the case" in subsection (i)(1), but the Rule is silent as to whether the court can award relief in a later case.

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[227] ECF No. 34 at 20–21.
[228] *Id.* (emphasis added) (citing FED. R. BANKR. P. 3002.1(i)(1)).
[229] FED. R. BANKR. P. 3002.1 advisory committee's note to 2011 adoption (emphasis added).
[230] ECF No. 37 at 17–18.
[231] FED. R. BANKR. P. 3002.1(i)(2).

This Court resists reading words into the Rule that do not appear there.[232] Thus, this Court looks to case law to determine whether Plaintiffs' Count III is appropriate in the instant case.

Neither party identified any case wherein the court held that a debtor could or could not seek relief for a Rule 3002.1 violation in a subsequent bankruptcy case. A review of case law reveals that there is one, non-binding case—*Finley*—wherein the bankruptcy court held that "claims for damages that arose during an active chapter 13 case must be pursed [sic] in an adversary proceeding filed in the case in which the violation or the other wrongful act occurred[.]"[233] In *Finley*, the debtor had filed three chapter 13 bankruptcy cases, one each in 2008, 2012, and 2015. The 2008 and 2012 cases were dismissed, but there was a pending adversary proceeding in the 2008 case. In that adversary proceeding, the court awarded the defendant partial summary judgment. Thereafter, the debtor filed a motion to supplement her complaint to add claims, including alleged violations of Rule 3002.1. Although the alleged violations occurred in the 2012 case, the debtor attempted to bring the Rule 3002.1 violations in the 2008 adversary proceeding, arguing that the defendant's conduct in the 2012 case was an extension of the conduct at issue in the 2008 case.

The *Finely* court denied the debtor's motion to supplement and limited the claims to events occurring during and with respect to the 2008 case. Using the debtor's stay violation claim as an example, the court explained that a stay violation in a previous case could be brought in a subsequent case if, for example, a creditor violated the stay by foreclosing on a debtor's property without obtaining stay relief, because then the debtor could raise a stay violation arguing that the sale was void and the property purportedly sold at the foreclosure sale was property of the estate in the

[232] *See Bates v. United States*, 522 U.S. 23, 29 (1997) ("[W]e ordinarily resist reading words or elements into a statute that do not appear on its face.").
[233] *Finley v. Carrington Mortg. Servs., LLC (In re Finley)*, 2016 Bankr. LEXIS 406, at *12 (Bankr. N.D. Ala. Feb. 9, 2016).

subsequent case.[234] However, the court concluded, "[c]laims seeking money damages for stay violations are in the nature of contempt for disobeying a court's order, and must be pursued in the case in which that order, e.g. the stay, was issued and not in a subsequent case or independent action" and cited to Rules 3001(c)(2)(D)(i)–(ii) and 3002.1(i)(1)–(2).[235]

In all other cases, the debtor either moved to reopen the bankruptcy case to assert a Rule 3002.1 violation after the debtor received a discharge and the case was closed,[236] or the debtor's prior bankruptcy case was dismissed, and the debtor brought the alleged violations in a subsequent case based on violations in both the prior and subsequent cases.[237] None of those cases discussed whether a debtor could bring a Rule 3002.1 violation in a subsequent bankruptcy case for violations occurring solely in the prior case, where the debtor previously received a discharge and the case was closed. Additionally, the allegations here are dissimilar to those in *Finley* in one important respect: Plaintiffs' Complaint alleges that Defendant's violations of Rule 3002.1 in the 2011 Case prevent it from collecting the payments and fees it seeks to collect in the present case, in part because Defendant misapplied funds in the previous case based on the undisclosed changes in payment.[238] Thus, Plaintiffs are seeking relief for continuing harm from Defendant's alleged violations of Rule 3002.1.

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[234] *Id.* at *12–13.
[235] *Id.* at *13 & n.8.
[236] *E.g.*, *Meyer v. Wells Fargo Bank, N.A. (In re Meyer)*, 2018 Bankr. LEXIS 1041, at *2 (Bankr. M.D. Pa. Apr. 4, 2018) (debtor received a discharge in her chapter 13 case and later filed a motion to reopen that case to allege, inter alia, that the creditor violated Rule 3002.1); *In re Longmire*, 2015 Bankr. LEXIS 3086, at *1, *5 (Bankr. W.D. Tenn. Sept. 11, 2015) (same); *Bivens v. New Rez LLC (In re Bivens)*, 625 B.R. 843, 846–47 (Bankr. M.D. N.C. 2021) (same); *Beiter v. Chase Home Fin., LLC (In re Beiter)*, 590 B.R. 446, 449 (Bankr. S.D. Ohio 2018) (same); *In re Polvorosa*, 621 B.R. 1, 2, 8, 16 (Bankr. Nev. 2020) (debtor brought a motion for contempt, which implicated Rule 3002.1 and the court found that relief under Rule 3002.1 was not appropriate).
[237] *E.g.*, *In re McCants*, 626 B.R. 80, 81 (finding that the creditor's claim survived after dismissal of the debtor's first bankruptcy case regardless of the creditor's failure to provide the Rule 3002.1 notice and the creditor's claim in the debtor's second bankruptcy case was not disqualified under Rule 3002.1).
[238] ECF No. 21 at 23–24, ¶¶ 102–103, 107, 109 (arguing that (1) because Defendant failed to file 3002.1(b) Notices of Payment Change in the 2011 Case, the purported payment changes are not enforceable against Plaintiffs; (2) Defendant misapplied payments made during the 2011 Case based on the undisclosed increases in Plaintiffs' monthly mortgage; (3) Defendant failed to file notices regarding fees, expenses, and other costs and cannot now collect on

Defendant's accounting errors in this case, Plaintiffs allege, stem from errors made in the 2011 Case.[239] For example, Plaintiffs' allege that Defendant's 410a attachment to its Claim No. 9-3 reflects Defendant's increase of the mortgage payment to $1,454 without the requisite Rule 3002.1(b) notice, which remained on Defendant's books until March 1, 2017.[240] The 410a attachment also contains fees and costs that were allegedly unnoticed in the 2011 Case, but that Defendant now seeks to recover.[241] Taking these allegations as true, Defendant committed accounting errors in the 2011 Case and is carrying those errors forward to its Claim No. 9-3. Those errors are impacting Plaintiffs' reorganization efforts in the present case. There is no binding authority on Rule 3002.1 that prohibits Plaintiffs from now seeking damages resulting from Defendant's alleged Rule 3002.1 violations in the prior case, particularly where Defendant is bringing allegedly improper payment change adjustments, accounting errors, and fees from the 2011 Case into the present case.

Accordingly, Plaintiffs may now, in their Complaint, bring the Rule 3002.1 violations from the 2011 Case.

c. Rule 3002.1(i) permits the award of sanctions and punitive damages if merited

Defendant argues that nothing in Rule 3002.1(i) indicates that "other appropriate relief" includes punitive monetary sanctions and moves to dismiss that request. Defendant again cites to *Tollstrup* wherein the court found that Rule 3002.1 does not permit the imposition of punitive monetary sanctions.[242] Plaintiffs argue that the advisory committee notes to Rule 3002.1 and this

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those omitted charges).
[239] *Id.* at 11–12, ¶ 52.
[240] *Id.* at 17–18, ¶ 81.
[241] *Id.* at 17, ¶ 80.
[242] ECF No. 34 at 21 (citing 2018 Bankr. LEXIS 767, at *13).

Court's decision in *Trevino II* permit punitive damages.[243] Before addressing Defendant's argument, this Court corrects Plaintiffs' mischaracterization of this Court's *Trevino II* opinion.

Plaintiffs' assertion that *Trevino II* supports the proposition that sanctions and/or punitive damages for violations of Rule 3002.1 and attendant abuse of the bankruptcy processes are appropriate is somewhat misleading. In *Trevino II*, this Court found that "the Plaintiffs' abuse of process claim and request for reasonable and necessary attorney's fees and expenses in relation thereto should be granted in an amount to be determined by this Court."[244] While that finding followed a discussion of the defendants' "actions, or lack thereof" regarding Rule 3002.1, the finding was solely as to the abuse of process claim under § 105(a).[245] This Court also found that the plaintiffs were entitled to punitive damages on their abuse of process claim, again under § 105(a).[246]

The plaintiffs in *Trevino II* did not request sanctions and punitive damages under Rule 3002.1(i) and therefore, this Court never reached that issue.[247] The plaintiffs did request reasonable, necessary fees and expenses under Rule 3002.1(i) and that request was denied because the plaintiffs alleged that the defendants Rule 3002.1 notice was incorrect, not that the defendants failed to provide notice. In denying that request, this Court explained that "Rule 3002.1(i) provides relief in situations involving a lack of notice, rather than incorrect notice."[248] Thus, after *Trevino II*, whether a court can assess sanctions and punitive damages under the Rule remained an open question. The Court considers that question now.

i. The Second Circuit's *Gravel* opinion

[243] ECF No. 21 at 18 (citing *Trevino v. HSBC Mortg. Servs. (In re Trevino)*, 615 B.R. 108, 128, 130–31 (Bankr. S.D. Tex. 2020)).
[244] *In re Trevino*, 615 B.R. at 131.
[245] *Id.* at 128–31.
[246] *Id.* at 145.
[247] *Id.* at 149.
[248] *Id.* at 146.

Although neither party here had the benefit of *Gravel* when Defendant's Motion was filed because it wasn't decided until August 2, 2021, this Court finds the dissenting opinion instructive. *Gravel* is the first circuit level opinion to decide the issue of punitive damages under Rule 3002.1.[249] And, as noted there, only two bankruptcy courts have considered the issue.[250] *Gravel* vacates one of those decisions and the other is *Tollstrup*, cited by Defendant.[251]

In *Gravel*, the chapter 13 trustee moved for sanctions against a mortgagee for violations of Rule 3002.1 in three separate cases.[252] After a consolidated hearing, the bankruptcy court granted the trustee's motions, ordering the mortgagee to pay $75,000 in punitive damages for violations of Rule 3002.1 and an additional $300,000 for violations of the court's orders pursuant to its § 105 powers.[253] The bankruptcy court "levie[d] this substantial penalty on [the mortgagee] to convey a clear message to [the mortgagee], and other mortgage creditors, that they may not violate court orders with impunity and will suffer significant monetary sanctions if they conduct their mortgage accounting operations in a manner that fails to fully comply with Rule 3002.1, violates court orders, or threatens the fresh start of Chapter 13 debtors."[254]

Both sanctions were vacated by the district court.[255] The district court remanded the matter, noting that the bankruptcy court could either refer the matter for criminal contempt proceedings or sanctions or could take steps to enforce its orders short of punitive sanctions of the scope and type imposed in the cases.[256] On remand, the bankruptcy court imposed the same $75,000 sanction for

[249] *PHH Mortg. Corp. v. Sensenich (In re Gravel)*, 2021 U.S. App. LEXIS 22752, at *18 (Aug. 2, 2021).
[250] *Id.*
[251] *Id.*
[252] *Id.* at *5–7.
[253] *Id.* at *7.
[254] *In re Gravel*, 556 B.R. 561, 580 (Bankr. D. Vt. 2016), vacated and remanded sub nom. *PHH Mortg. Corp. v. Sensenich*, 2017 U.S. Dist. LEXIS 207801 (D. Vt. Dec. 18, 2017).
[255] *PHH Mortg. Corp.*, 2017 U.S. Dist. LEXIS 207801, at *24–25 (D. Vt. Dec. 18, 2017).
[256] *Id.* at *25.

the violations of Rule 3002.1 and reduced the $300,000 sanction by 25%.[257] The mortgagee appealed to the district court, but the trustee requested that the bankruptcy court certify its order for the direct review of the Second Circuit Court of Appeals.[258] That request was granted and the trustee petitioned to the Second Circuit, which granted review.[259]

a. The majority's opinion

Relevant to the instant case, by a 2-1 decision the circuit court vacated and reversed the $75,000 punitive damages award for violations of Rule 3002.1.[260] The majority's first basis for vacating the sanction was that the phrase "other appropriate relief" in Rule 3002.1(i)(2) is a general phrase among specific examples and should be "construed in a fashion that limits the general language to the same class of matters as the things illustrated."[261] Reasonable attorney's fees and expenses, that "expressly remedy harms to the debtor 'caused by the [creditor's] failure,' to give notice of a claim[,]" the majority reasoned, are compensatory forms of relief, suggesting that "other appropriate relief" is limited to non-punitive sanctions.[262] Likewise, the relief set forth is subdivision (i)(1), the majority continued, is not a punishment because it permits the court to prevent the creditor from collecting an un-noticed amount only if the non-compliance caused harm, "serv[ing] the remedial goal of shielding the debtor from unforeseen charges," so that the debtor's fresh start is not later disrupted. Thus, the court concluded, subdivision (i)(1) reinforces the inference that "other appropriate relief" is limited to non-punitive sanctions.[263]

[257] *In re Gravel*, 2021 U.S. App. LEXIS, at *9.
[258] *Id.*
[259] *Id.*
[260] *Id.* at *26–27.
[261] *Id.* at *19 (quoting *Canada Life Assurance Co. v. Converium Ruckversicherung (Deutschland) AG*, 335 F.3d 52, 58 (2d Cir. 2003)).
[262] *Id.*
[263] *Id.* at *20.

The majority's second basis for vacating the $75,000 sanction was that in contrast with Rule 3002.1(i), there are sections of the Bankruptcy Code—namely § 362(k)(1)—that explicitly provide for punitive damages in appropriate circumstances.[264] The majority also disagreed with the bankruptcy court's reasoning that the mere preclusion of evidence and award of attorney's fees would be insufficient to deter violations of Rule 3002.1, drawing an analogy to discovery sanctions pursuant to FRCP 37.[265] Finding the analogy unpersuasive, the majority reasoned that discovery sanctions under FRCP 37 are meant as deterrents to punish recalcitrant or evasive parties for the protection of the interests of the parties, the court, and the public in a speedy and just resolution of the case.[266] Contrarily, Rule 3002.1 solely aims to protect the debtor's interest. FRCP 37, the majority continued, permits imposition of a range of sanctions, including "further just orders."[267] Rule 3002.1 does not authorize "just orders."[268] The majority concluded that "[t]he sanction was imposed under Rule 3002.1(i), and our holding is that the sanction went beyond the relief authorized by that rule."[269]

b. The dissent's opinion

The dissenting judge disagreed, concluding that "the plain meaning of 'other appropriate relief' under Rule 3002.1, as confirmed by its modeling after both [FRCP] 37 and that Rule's purpose, authorizes a bankruptcy court to use its discretion to impose punitive monetary sanctions in appropriate circumstances for violations of Rule 3002.1."[270] The dissent began with the plain language of Rule 3002.1(i). Focusing on the word "including," the dissent noted that pursuant to

[264] *Id.* (citing 11 U.S.C. § 362(k)(1) ("[A]n individual injured by any willful violation of a stay provided by this section shall recover actual damages, including costs and attorneys' fees, and, in appropriate circumstances, may recover punitive damages.")).
[265] *Id.* at *20–21.
[266] *Id.* at *21.
[267] *Id.* at *22.
[268] *Id.*
[269] *Id.* at *23.
[270] *Id.* at *30, *50–51.

11 U.S.C. § 102(3) subdivision (i)(2) should be interpreted to mean "including, but not limited to" compensatory relief.[271]

Next, the dissent pointed out that the classification by the majority of the evidence-preclusion in (i)(1) as a "non-punitive sanction" is inaccurate because such preclusion is not designed to be proportionate to the harm caused, but rather is meant to deter future violations of Rule 3002.1.[272] As the Second Circuit noted in another context, "the preclusion of evidence can be a *more extreme* sanction than monetary sanctions" and is particularly important because of its punitive nature and deterrent effect.[273] Thus, the dissent deduced, the evidence-preclusion provision of Rule 3002.1(i) "is properly classified as a potentially punitive sanction that also operates as a deterrent."[274] Relying on the "same class of matters" canon employed by the majority, "other appropriate relief" necessarily includes punitive monetary sanctions because evidence preclusion is a punitive sanction meant to deter.[275]

The dissenting opinion also compared Rule 3002.1 to FRCP 37(c)(1), after which the Rule was modeled.[276] In relevant part, FRCP 37(c)(1) contains an evidence-preclusion sanction and states that if a party fails to adhere to FRCP 26(a) or (e), then the court: "(A) may order payment of the *reasonable expenses including attorney's fees*, caused by the failure . . . and (C) may impose *other appropriate sanctions, including* any of the orders listed in Rule 37(b)(2)(A)(i)-(vi)."[277] And although the Second Circuit has never decided whether punitive damages can be assessed under FRCP 37, the dissent agreed with the majority of courts that they could be under the "other

[271] *See id.* at *35.
[272] *Id.* at *36–37.
[273] *Id.* at *37–38 (first citing *Cine Forty-Second St. Theatre Corp. v. Allied Artists Pictures Corp.*, 602 F.2d 1062, 1066 (2d Cir. 1979) then citing *Daval Steel Prods. v. M/V Fakredine*, 951 F.2d 1357, 1365-67 (2d Cir. 1991) finally citing *Nat'l Hockey League v. Metro. Hockey Club*, 427 U.S. 639, 643, 96 S. Ct. 2778, 49 L. Ed. 2d 747 (1976)).
[274] *Id.* at *38.
[275] *Id.* at *38–39 (citing *Canada Life Assurance Co.*, 335 F.3d at 58).
[276] *Id.* at *40–41.
[277] *Id.* at *40 (citing FED. R. CIV. P. 37(c)(1) (emphases added)).

appropriate sanctions" language of the rule.[278] Rule 3002.1(i)(2), the dissent continued, contains the same "other appropriate relief" language, which operates as a "catch-all provision" in both rules, intended to "cloak the court with the flexibility and discretion to impose unenumerated punitive sanctions[.]"[279] The dissent disagreed with the majority's distinguishment between FRCP 37 and Rule 3002.1 on the basis that the former protects the parties, the court, and the public whereas the latter solely protects the debtor. While Rule 3002.1 protects the debtor, it is equally important to the bankruptcy courts and the public who have an interest in ensuring that the "fresh start" objective of the Bankruptcy Code is not undermined, and that speedy and just resolutions of chapter 13 cases take place.[280]

Lastly, the dissent considered the purpose behind the enactment of Rule 3002.1.[281] Prior to Rule 3002.1, mortgagees, without notice to the debtor, would add fees and costs to the debtor's mortgage during the pendency of the bankruptcy case.[282] After the bankruptcy case ended, mortgagees attempted to foreclose on debtors based on those post-petition defaults for which they assessed fees.[283] Rule 3002.1 was adopted to remedy that problem by requiring the mortgagee to give both the debtor and the trustee notice of fees and payment changes during the bankruptcy case.[284] To limit the remedies permitted under Rule 3002.1 to compensatory awards would likely render that provision an insufficient deterrent, where the fees assessed by mortgagees are often relatively small and either go unnoticed by debtors or debtors choose not to fight them.[285] Without the possibility of punitive damages, mortgagees have little incentive to make the systemic changes

[278] *Id.* *40–41.
[279] *Id.* at *42.
[280] *Id.* at *49.
[281] *Id.* at *42–50.
[282] *Id.* at *43.
[283] *Id.*
[284] *Id.*
[285] *Id.* at *47–49 (citing Nat'l Assoc. of Chapter 13 Trs. Amicus Br. at 5–6, 15).

required to service loans properly in chapter 13.[286] For those reasons, the dissent concluded that Rule 3002.1(i)(2) permits bankruptcy courts to use their discretion to impose punitive monetary sanctions.[287]

ii. The plain language of Rule 3002.1(i) and the policies underlying the Bankruptcy Code permit punitive damages and sanctions as "other appropriate relief" under Rule 3002.1(i)(2)

This Court respectfully disagrees with the majority and agrees with the dissent. The plain language of Rule 3002.1(i) places few restrictions on the types of remedies bankruptcy courts can issue. First, under subdivision (i)(1), a court is only prohibited from precluding evidence if the creditor's failure was substantially justified or harmless. Second, under subdivision (i)(2), the relief the court can award is only limited to that which is "appropriate." Thus, the plain language of Rule 3002.1(i) provides courts significant latitude in awarding sanctions. Additionally, as discussed by the dissent in *Gravel*, the word "including," as used in the Rule, is not limiting.[288] Reasonable expenses and attorney's fees are merely two examples, not an exhaustive list.

Beyond the plain language, this Court cannot conclude from the enumerated examples in (i)(2) that courts should be limited to compensatory relief. Evidence preclusion is a particularly harsh punitive sanction, warranted only under rare circumstances.[289] Reasonable expenses and attorney's fees do not conclusively establish that only compensatory awards are appropriate either. The explicit mention of attorney's fees is necessary for courts to depart from the American Rule

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[286] *Id.*
[287] *Id.* at *50–51.
[288] 11 U.S.C. § 102(3).
[289] *See, e.g.*, *Symetra Life Ins. Co. v. Rapid Settlements, Ltd.*, 2012 U.S. Dist. LEXIS 166238, at *36 (S.D. Tex. Nov. 21, 2012 ("While Rule 26 violations may warrant evidence preclusion, it is, or can be, a harsh sanction.") (reversed on other grounds), *aff'd in part, rev'd in part*, 775 F.3d 242 (5th Cir. 2014); *Update Art, Inc. v. Modiin Publ'g, Ltd.*, 843 F.2d 67, 71 (2d Cir. 1988) ("The harshest sanctions available [under FRCP 37] are preclusion of evidence and dismissal of the action"); *R & R Sails, Inc. v. Ins. Co. of the Pa.*, 673 F.3d 1240, 1247 (9th Cir. 2012) ("Yet evidence preclusion is, or at least can be, a harsh sanction.") (cleaned up).

when considering fee shifting[290] and therefore provides little indication as to how courts should interpret "other appropriate relief."

Permitting sanctions and punitive damages as "other appropriate relief" under Rule 3002.1(i)(2) also best serves the policy goals underlying the bankruptcy system. It is well recognized that a creditor's failure to comply with the notice requirements of Rule 3002.1 can hinder the honest debtor's right to a fresh start following bankruptcy.[291] Punitive damages protect that right by deterring violations of the Rule that threaten a fresh start. Punitive damages could likewise curtail repeat bankruptcy filings, thereby conserving both judicial resources and the parties' resources. Where the debtor's fresh start is defiled by Rule 3002.1 violations, the likelihood of a subsequent bankruptcy filing is greater than zero. This case serves as an example. Plaintiffs allege that throughout their 2011 Case they paid $1,197 as designated in their 2011 Plan and as ordered by this Court, but Defendant repeatedly changed the payment amount—from $1,276 to $1,195 to $1,454—and added fees and costs without notice.[292] Those occurrences, in conjunction with others, caused accounting errors that resulted in Defendant sending default notices to Plaintiffs beginning August 31, 2017, before Plaintiffs received their discharge in the 2011 Case.[293] Shortly after Plaintiffs received their discharge, they became frustrated by Defendant's post-discharge activity and stopped making payments on the mortgage.[294] Defendant continued to send delinquency notices and eventually sought foreclosure.[295] Plaintiffs filed the instant bankruptcy case to halt

[290] *Baker Botts L.L.P. v. ASARCO LLC*, 576 U.S. 121, 126 (2015) ("We have recognized departures from the American Rule only in 'specific and explicit provisions for the allowance of attorneys' fees under selected statute.") (*quoting Alyeska Pipeline Serv. Co. v. Wilderness Society*, 421 U.S. 240, 260 (1975)).
[291] *See, e.g.*, *In re Tavares*, 547 B.R. at 214 (recognizing that the creditor's failure to following Rule 3002.1 can defile a debtor's fresh start with a surprise attack at the conclusion of the case); *In re Rivera*, 599 B.R. 335, 342 (Bankr. D. Ariz. 2019) ("The Rule is a 'procedural mechanism designed to effectuate the Chapter 13 policy of providing debtors with a fresh start.'") (quoting *In re Thongta*, 480 B.R. 317, 319 (Bankr. E.D. Wis. 2012)).
[292] ECF No. 21 at 17–18, ¶ 81.
[293] *Id.* at 17, ¶ 77.
[294] *Id.* at 15–16, ¶ 71.
[295] *Id.* at 17, ¶ 78.

foreclosure.[296] Taking those allegations as true, Plaintiffs' fresh start was spoiled, in part, by Defendant's violations of Rule 3002.1, resulting in Plaintiffs once again knocking on the courtroom door.

Moreover, the consumer bankruptcy process "is vulnerable to opportunistic behavior" and "[s]ome repeat players - large lenders and servicers with thousands of borrowers in bankruptcy - may take advantage of the lack of direct oversight to extract undue benefits from the bankruptcy system."[297] Under the appropriate circumstances, courts may use punitive sanctions to curb opportunistic behavior. As Kara Bruce explains in her article:

> Even if a consumer is aware that her rights have been violated, the damages available to that individual consumer are often too small to justify the costs of litigating a matter. These include not only direct costs (hiring an attorney and paying filing fees, for example), but also the time and effort it takes to locate an attorney, confirm that a legal claim exists, and commence suit. Even if a consumer can surmount these hurdles, the amount she is able to invest in a suit might well be dwarfed by the investment of a company that profits from perpetuating the harm on similarly situated consumers. These financial barriers to private litigation can theoretically be addressed by the imposition of litigation incentive, such as statutory or punitive damages, fee-shifting rules, and damage multipliers.[298]

The dissent in *Gravel* echoes this sentiment. Costs and attorney's fees alone may be an insufficient deterrent because the fees and charges that violate Rule 3002.1 may either go unnoticed by the debtor or the debtor will find it easier to pay the small fees rather than litigate them.[299] This permits Rule violators to escape sanction altogether.[300] It is precisely because many of the fees that violate Rule 3002.1 are small that punitive damages should be levied in the appropriate case.

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[296] *Id.* at 4, ¶ 5.
[297] Kara Bruce, *Closing Consumer Bankruptcy's Enforcement Gap*, 69 Baylor L. Rev. 479, 480 (2017).
[298] *Id.* at 502–03.
[299] *In re Gravel*, 2021 US App LEXIS at *47.
[300] *Id.*

Accordingly, sanctions and punitive damages may be assessed under Rule 3002.1(i)(2) as "other appropriate relief" where circumstances warrant. Plaintiffs must nevertheless satisfy their evidentiary trial burden to prove they are entitled to such relief.

d. Plaintiffs have no duty to allege harm under Rule 3002.1(i)

In the alternative, Defendant moves to dismiss Plaintiffs' Count III on the bases that (1) Plaintiffs have not alleged that they suffered harm as a result of Defendant's alleged Rule 3002.1 violations; and (2) elimination of a lien or of any contractual obligations is not an appropriate remedy under Rule 3002.1(i)(2). Plaintiffs' Complaint seeks actual damages, attorneys' fees and costs, and any other appropriate relief, including substantial punitive damages and/or sanctions.[301] Plaintiffs' Count III does not ask this Court to "eliminate" Defendant's lien or any contractual obligations.[302] The Complaint asks this Court to award "other appropriate relief," but does not specify what that relief might be.[303] At this stage in the proceeding, this Court will not assume that Plaintiffs' general request is a request to "eliminate" the lien or any contractual obligations.

Accordingly, Defendant's request to dismiss on the basis elimination of a lien or of any contractual obligations not being an appropriate remedy under Rule 3002.1(i)(2) is denied.

Additionally, Rule 3002.1 does not require Plaintiffs to allege harm to be entitled to "other appropriate relief, including reasonable expenses and attorney's fees"[304] and Defendant provides no support for its claim that the Rule does. Rule 3002.1(i) says that a court *may* either preclude the holder of a claim from presenting the omitted information as evidence or award other appropriate relief or both. The use of "may" indicates that a court has discretion.[305] The plain language

[301] ECF No. 21 at 25, ¶ 114.
[302] *Id.* at 22–25, ¶¶ 97–114.
[303] *Id.* at 25, ¶ 114.
[304] FED. R. BANKR. P. 3002.1(i)(2).
[305] *Jama v. Immigration & Customs Enf't*, 543 U.S. 335, 346 (2005).

of the Rule imposes three restrictions on that discretion: (1) the court must provide notice and a hearing; (2) to preclude evidence, the court must determine that the failure to comply with the Rule caused harm and was not substantially justified; and (3) "other relief" must be appropriate.[306]

The second restriction does not apply to the court's discretion to award other appropriate relief, including reasonable expenses and attorney's fees under subdivision (i)(2). Rule 3002.1(i) does not require courts to find that harm was caused by a claim holder's failure to adhere with the notice requirements of the Rule.[307] The decision to impose sanctions rests solely with the court, after notice and hearing.[308] This does not mean that the court is prohibited from considering whether the failure was substantially justified or caused harm. It simply means that such consideration is not required when considering "other appropriate relief."

However, even if the Rule required Plaintiffs to demonstrate harm, Plaintiffs' Complaint pled facts from which this Court can make a reasonable inference that Defendant's conduct harmed Plaintiffs. Plaintiffs allege that because Defendant failed to provide notice of the payment changes, Plaintiffs were stripped of the opportunity to object to those changes.[309] Plaintiffs also allege that Defendant misapplied payments based on the unnoticed payment changes and fees, sent numerous delinquency notices, and eventually sought foreclosure, causing Plaintiffs to seek bankruptcy relief.[310] Plaintiffs' admission that they stopped making payments to Defendant after November 2018 has no bearing on whether Defendant's alleged violations caused them harm.

Accordingly, this Court finds that Rule 3002.1(i)(2) does not require Plaintiffs to plead harm and, even if it did, Plaintiffs have pled a plausible claim for relief.

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[306] FED. R. BANKR. P. 3002.1(i).
[307] *Id.*; *see also Meyer v. Wells Fargo Bank, N.A. (In re Meyer)*, 2018 Bankr. LEXIS 1041, at *33 (Bankr. M.D. Pa. Apr. 4, 2018).
[308] See Note 307 *supra*.
[309] ECF No. 21 at 23, ¶ 101.
[310] *Id.* at 1, 24–25, ¶¶ 77–79, 109–110.

3. Plaintiffs' Counts V–VIII

Finally, Defendant posits that Plaintiffs have not sufficiently alleged harm or damages resulting from Defendant's alleged violations for Plaintiffs' Counts V through VIII. For each of these counts, Plaintiffs request that the Court impose monetary sanctions against Defendant.[311] Defendant, in sum, asserts that while Counts V–VIII of Plaintiffs' Complaint allege wrongful conduct based on Defendant's alleged misapplication of payments, Plaintiffs do not allege facts that, taken as true, demonstrate that Defendant's violation of the chapter 13 plan, the automatic stay, the discharge injunction, or the other Court orders in the 2011 Case caused any actual damages.[312] As such, Defendant asks this Court to dismiss Counts V–VIII.

Counts V–VIII are based on a core set of allegations summarized here. Plaintiffs' Complaint alleges that: (1) Defendant failed to bring its books and records in accordance with this Court's Deem Current Order in the 2011 Case, continuing to assess a balance of $3,885.93 in fees and charges, $1,072.17 in an unapplied funds balance, and $1,716.03 in a negative escrow balance; (2) Defendant increased the monthly mortgage payment to $2,012 on March 1, 2017, and assessed that balance, plus corresponding accruals of interest, escrow deficiencies, and other such fees based on the $2,012 rate until September 4, 2020, when Defendant lowered the monthly mortgage amount to $1,453.39 without explanation; (3) the increase to $2,012 was allegedly due to an increase in taxes or insurance, but Plaintiffs were paying the Property insurance themselves and the county tax entities reflect no increase in taxes on the Property for that period; (4) Defendant was paying insurance on a different property owned by Plaintiffs and improperly adding the insurance costs to the Property; (5) Defendant carried forward incorrect escrow deficiency amounts from the 2011 Case and then on September 4, 2019, credited that portion of Plaintiffs' mortgage account in

[311] *Id.* at 30, 32–34, ¶¶ 143, 154, 160, 166.
[312] ECF No. 34; ECF No. 21 at 29, ¶ 136.

the amount of $13,900.35 for an "insurance refund"; (6) Defendant assessed "Bankruptcy Fees" and "Bankruptcy Costs" totaling $2,150 to Plaintiffs' mortgage account on September 27, 2019, at a time when Plaintiffs were not in bankruptcy; and (7) Defendant assessed litigation costs against Plaintiffs after the Deem Current Order and the discharge were entered based largely on the wrongful assessment of an incorrect monthly payment amount that Plaintiffs were not contractually obligated to pay.[313] The Court will consider each in turn.

a. Count V (Defendant's alleged violation of the plan and order confirming the plan)

Count V of Plaintiffs' Complaint alleges that Defendant "violated 11 U.S.C. § 1327 and other provisions of the Code and Rules, Plaintiffs' confirmed Chapter 13 plan, the orders confirming the plan, 11 U.S. C. § 541(i), and other motions, directives, and orders of the Court."[314] The aforementioned Code sections are silent on the issue of damages. Plaintiffs maintain that "under § 105 and/or the Court's inherent authority, Defendant should be sanctioned in an appropriate amount and made to pay Plaintiffs' reasonable attorneys' fees for bringing this action."[315] Defendant objects, pointing out that under Count V, Plaintiffs are seeking a broad swath of damages, including "mental anguish, emotional distress, actual damages, nominal and incidental damages, mileage damages, reputational damages, lost equity, damage to credit, and attorneys' fees and costs."[316] Defendant contends that Plaintiffs allege no facts evidencing specific harm as the result of Defendant violating any of the Court's Orders. This Court disagrees.

A confirmed plan constitutes a new arrangement between the debtor and creditors and a claim may arise from the confirmed plan.[317] Specifically, § 1327 binds the debtor and each creditor

[313] ECF No. 21 at 18–19, ¶¶ 82–86.
[314] *Id.* at 29, ¶ 137.
[315] *Id.* at 30, ¶ 143.
[316] ECF No. 34; ECF No. 21 at 30, ¶ 142.
[317] *In re Cano*, 410 B.R. 506, 524 (Bankr. S.D. Tex. 2009); *In re Stratford of Tex., Inc.*, 635 F.2d 365, 368 (5th Cir.1981).

to the provisions of a confirmed plan.[318] Section 105 grants courts broad authority to enter any order or judgment "necessary or appropriate to carry out the provisions" of the Bankruptcy Code.[319] Courts have used this broad authority to remedy violations of confirmed plans.[320] A bankruptcy court's authority under § 105 to enforce its own orders cannot be reasonably questioned.[321] As such, allowing debtors to seek damages for violations of court orders confirming chapter 13 plans enforces rights.[322] This use of § 105 is a remedy to enforce rights incorporated by the confirmed plans.

Accordingly, application of the Court's § 105 power to provide some or all the remedies sought by Plaintiffs may be appropriate if Plaintiffs prove the facts pled.[323]

Plaintiffs pled that "[Defendant] failed to apply Plaintiffs' payments to their mortgage loan account in the correct amounts and/or applied payments to improper and undisclosed fees and expenses in violation of bankruptcy law."[324] Plaintiffs' Complaint outlines the discrepancies between the amounts set forth in this Court's Agreed Order[325] in the 2011 Case and the proof of claim filed by Defendant encompassing the same time period.[326] Count V repeats and realleges the other allegations in the Complaint, which outline the payment misapplications relating to

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[318] 11 U.S.C. § 1327.
[319] *Id.* § 105(a).
[320] *In re Cano*, 410 B.R. 506, 540 (Bankr. S.D. Tex. 2009).
[321] *Id.*; *Am. Airlines Inc. v. Allied Pilots Ass'n*, 228 F.3d 574, 585 (5th Cir.2000) ("Judicial sanctions in civil contempt proceedings may, in a proper case, be employed for either or both of two purposes: to coerce the defendant into compliance with the court's order, and to compensate the complaint for losses sustained.") (quoting *U.S. v. United Mine Workers of Am.*, 330 U.S. 258, 303–04, 67 S.Ct. 677, 91 L.Ed. 884 (1947)); *Musslewhite v. O'Quinn (In re Musslewhite)*, 270 B.R. 72, 79 (S.D.Tex.2000) ("The Bankruptcy Court's finding of civil contempt and that Court's exercise of discretion to impose sanctions to compensate O'Quinn for Debtor's repeated and blatant violations of the Bankruptcy Court's various orders are not clearly erroneous.*"); Sanchez v. Ameriquest Mortgage Co. (In re Sanchez)*, 372 B.R. 289, 317 (Bankr.S.D.Tex.2007) (holding that "the Defendant has violated the Court's order approving the Amended Plan, and the Defendant may be sanctioned for civil contempt"); *Tate v. NationsBanc Mortgage Corp. (In re Tate)*, 253 B.R. 653, 669 (Bankr.W.D.N.C.2000); *In re Padilla*, 379 B.R. at 643 (the court considered the extent to which the Bankruptcy Code provides relief for violations of an order confirming a plan.
[322] *In re Cano*, 410 B.R. at 541.
[323] *Id.*
[324] ECF No. 21 at 29, ¶ 136.
[325] *Id.* at 12–13, ¶¶ 55 –57; *see* 11-70475, ECF No. 91.
[326] *Id.* at 17–19, ¶¶ 80–86.

undisclosed fees and expenses that Defendant unlawfully charged to Plaintiffs' account.[327] Plaintiffs state that "many of the fees, expenses, and other costs still carried on the books and records of Community are fees and expenses and costs it did not disclose in the [Plaintiffs'] 2011 Case but which were aggressively assessed in the intervening years between the two chapter 13 cases and which are now being used to collect in this case."[328] In essence, Plaintiffs pled that Defendant's actions are in contravention of this Court's orders entered in the 2011 Case. As stated by the court in *Cano*, "[t]he Court would be ignoring the plain congressional intent of § 105 and editing-out words from § 105 if the Court dismissed Plaintiffs' complaint at this early stage. The Court cannot yet discern what is necessary or appropriate. The story is yet to be told."[329] The Court is not willing to foreclose the possibility that it may award damages should Plaintiffs prove up their case at trial, and Defendant is on more than sufficient notice to defend against such claims.

Accordingly, Defendant's Motion to Dismiss Plaintiffs' Count V is denied.

b. Count VI (willful violation of the automatic stay)

Under Count VI, Plaintiffs assert that Defendant's actions constitute willful violations of the automatic stay as set forth in 11 U.S.C. § 362(a)(3). Defendant objects by pointing out that Plaintiffs allege only conclusory "damages as a result of Community's violation of the automatic stay."[330] In response, Plaintiffs contend that Defendant violated the stay by (a) applying Plaintiffs' 2011 Plan payments to wrongful fees, (b) filing a proof of claim that included an alleged pre-petition escrow shortage and subsequently collecting monthly mortgage payments including the same amounts, (c) changing monthly mortgage payment amounts without filing a respective 3002.1(b) Notice of Payment Change, and (d) not bringing its books and records in conformity

[327] See *id.* at 17–19, 22–35, ¶¶ 80–86, 97–174.
[328] *Id.* at 24, ¶ 109 (Plaintiffs incorporated this portion of the Complaint into Count V).
[329] *In re Cano*, 410 B.R. at 543.
[330] ECF No. 34.

with this Court's Deem Current Order in the 2011 Case and continuing to assess a balance of $3,855.93 in fees and charges and ($1,072.17) in unapplied funds balance.[331] Each allegation contained in Count VI of Plaintiffs' Complaint begins with "Community violated the stay in the Previous Case by . . . ."

Further, § 362(k)(1) delineates ". . . an individual injured by any willful violation of a stay provided by this section shall recover actual damages, including costs and attorneys' fees, and, in appropriate circumstances, may recover punitive damages."[332] Plaintiffs' Complaint states "Defendant is liable to Plaintiffs for Plaintiffs' actual damages, punitive damages, and reasonable attorneys' fees and costs caused by [Defendant's] willful stay violations. 11 U.S.C. § 362(k)."[333] Considering the facts set forth in the Complaint in conjunction with Plaintiffs' explicit request for damages modeled under the applicable statute, the Court finds that Plaintiffs pled enough to survive Defendant's Motion to Dismiss.

Accordingly, Defendant's Motion to Dismiss Plaintiffs' Count VI is denied.

c. Count VII (violation of the discharge injunction)

Plaintiffs' Count VII asserts that Defendant violated 11 U.S.C. § 524(i) by failing to properly apply funds received from the Plaintiffs and the chapter 13 trustee in accordance with the provisions of Plaintiffs' confirmed 2011 Plan. Defendant objects, arguing that Plaintiffs' allegations that they "have suffered material injury due to Defendant's willful failure to credit Plaintiffs' payments pursuant to their confirmed plan in their previous bankruptcy case" and "have incurred damages, including attorneys' fees and out-of-pocket expenses, amongst others, and have suffered

[331] ECF No. 21 at 30–31, ¶¶ 147–150; *see also id.* ¶¶ 115–132 (describing allegedly unlawful and undisclosed charges assessed by Defendant, which allegations are repeated and realleged by reference in Count VI).
[332] 11 U.S.C. § 362(k)(1).
[333] ECF No. 21 at 32, ¶ 154.

emotional distress" are conclusory.[334] Defendant contends that Plaintiffs do not allege facts that, if taken as true, would demonstrate that Defendant's violation of the discharge injunction caused any actual damages.[335]

Section 524(i) provides that:

> The willful failure of a creditor to credit payments received under a plan confirmed under this title, unless the order confirming the plan is revoked, the plan is in default, or the creditor has not received payments required to be made under the plan in the manner required by the plan (including crediting the amounts required under the plan), shall constitute a violation of an injunction under subsection (a)(2) if the act of the creditor to collect and failure to credit payments in the manner required by the plan caused material injury to the debtor.

In essence, it provides a post-discharge remedy for debtors.[336] Further, because the Court has the power to enforce its own orders, Plaintiffs are permitted to sue pursuant to § 105 for violations of the Court's orders and the § 524(i) discharge provision.[337] As discussed *supra*, debtors who sue based on violations of court orders are simply asking the court to use the power granted by § 105 to enforce its own orders.[338]

Here, Plaintiffs allege that they suffered material injury because of Defendant's willful failure to credit Plaintiffs' payments pursuant to their confirmed 2011 Plan and because of Defendant's misapplication of payments.[339] Plaintiffs contend that by failing to credit Plaintiffs' payments as required by the 2011 Plan, Defendant diverted such payments to amounts not actually owed under bankruptcy law, causing financial injury.[340] Plaintiffs assert that Defendant's failure to comply with § 524(i) ultimately forced Plaintiffs to file the current bankruptcy case, causing them to incur additional attorneys' fees and pay additional fees to the chapter 13 trustee in

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[334] ECF No. 34 at 24; *see* ECF No. 21 at 32–33, ¶ 159.
[335] ECF No. 34 at 24.
[336] *In re Parkman*, 589 B.R. 567, 577 (Bankr. S.D. Miss. 2018).
[337] *See In re Pompa*, 2012 WL 2571156, at *5 (Bankr. S.D. Tex. June 29, 2012).
[338] *Id.*
[339] ECF No. 37.
[340] ECF No. 21 at 32–33, ¶ 159.

connection with this case.[341] Assuming the facts pled are true and incorporating the facts referenced herein, collection and failure to credit payments in the manner required in the 2011 Case may have caused injury to the Plaintiffs, entitling them to post-discharge relief. At a minimum, Plaintiffs pled enough facts to have their day in court on this issue.

Accordingly, Defendant's Motion to Dismiss Plaintiffs' Count VII is denied.

d. Count VIII (contempt)

Plaintiffs' Count VIII asks this Court to find Defendant in contempt as a result of the alleged actions taken by Defendant referenced herein.[342] In its Motion, Defendant cites to the proposition that "[s]anctions for civil contempt may be imposed for either of two purposes: (i) to coerce compliance with a court order or injunction; or (ii) to compensate for damages sustained because of the contemptuous conduct."[343] Defendant argues that justification for an award of damages on a cause of action and an award of damages in the form of civil sanctions differ.[344] According to Defendant, the justification for the former is conduct that violates a common law or statutory duty or promise, whereas the justification for the latter is conduct that violates a court order or injunction. Defendant argues that sanctions for civil contempt for violating the automatic stay cannot be a substitute for damages available at law, and the remedy imposed by a court must have some connection between the harm alleged and the damages or remedy a plaintiff seeks to recover. And so, the argument goes, because Defendant asserts that Plaintiffs are not seeking an order compelling Defendant to comply with the Court's previous orders and make no allegation that Defendant is still not in compliance with any order, this Count should be dismissed.

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[341] *Id.*
[342] ECF No. 21 at 34.
[343] ECF No. 34; *In re Hester*, 554 B.R. 143, 147 (Bankr. N.D. Tex. 2016) (citing *United States v. United Mine Workers of Am.*, 330 U.S. 258, 303–04 (1947).
[344] ECF No. 34 at 23.

However, § 105 authorizing the court to issue any order necessary or appropriate to carry out the provisions of title 11 is not but a statutory codification and supplantation of bankruptcy courts' inherent civil contempt authority; bankruptcy courts have both inherent contempt authority and equitable authority under the statute.[345] This Court will not inhibit its authority to make a finding of contempt. It remains to be seen whether a finding is necessary or appropriate. As pled, Plaintiffs' allegations are plausible enough to defeat the pending Motion to Dismiss.

Accordingly, Defendant's Motion to Dismiss Plaintiffs' Count VIII is denied.

B. Plaintiffs' Motion to Dismiss

Plaintiffs move to dismiss Defendant's Counterclaims I and II. Plaintiffs assert that Defendant's Counterclaim I for breach of contract should be dismissed because (i) it is redundant and procedurally improper to bring the breach of contract claim in this proceeding;[346] (2) Defendant failed to satisfy the pleading requirements of FRCP 8(a) regarding damages;[347] and (iii) Defendant has not pled that the alleged breach was material.[348] Plaintiffs also allege that Defendant's Count II fails to state a claim because Defendant has not pled facts showing that it is entitled to relief from the automatic stay and has not sufficiently pled that it is the holder of the Note and Deed of Trust.[349]

1. Defendant's Counterclaim I (breach of contract)

Defendant's first counterclaim alleges that Plaintiffs breached section 2.4 of the Deed of Trust by failing to make the required payments as they became due, section 3.1 of the Deed of Trust by failing to maintain insurance on the Property from October 8, 2018, through September

[345] *In re Cano*, 410 B.R. 538–39 (first citing *In re Yorkshire*, 540 F.3d 328, 332 (5th Cir.2008) ("It is well-settled that a federal [bankruptcy] court, acting under inherent authority, may impose sanctions against litigants or lawyers. . . .") then citing *In re Jove Eng'g, Inc. v. IRS*, 92 F.3d 1539, 1553 (11th Cir. 1996)).
[346] ECF No. 36 at 6–9, ¶¶ 23–33.
[347] *Id.* at 2, ¶¶ 2–3.
[348] *Id.* at 7, ¶ 27.
[349] *Id*. at 2–3, ¶¶ 4–5.

23, 2019, and section 3.9 of the Deed of Trust by failing to maintain the Property in a good and safe condition of repair.[350] Defendant further alleges that Plaintiffs breached section 18 of the Note and section 5.10 of the Deed of Trust by using the Property for personal purposes, rather than business purposes.[351] Defendant alleges that it suffered actual damages and that Plaintiffs are $33,607.60 in arrears.[352] Plaintiffs ask this Court to dismiss Defendant's Counterclaim I.

a. Defendant's counterclaim for breach of contract is not redundant or procedurally improper

Plaintiffs argue that Defendant's breach of contract claim should be dismissed because this proceeding contains a claim objection and Defendant's counterclaim is outside the scope of an objection.[353] Plaintiffs also contend that this Court's order applied only certain adversary rules to this "contested matter," which did not include Federal Rule of Bankruptcy Procedure 7013, the rule governing counterclaims and cross-claims.[354]

It is true that this proceeding was born out of Plaintiffs' Objection to Defendant's Claim No. 9-2, since amended to 9-3. It is also true that this Court upon Plaintiffs' request, ordered that certain adversary proceeding rules apply to Plaintiffs' Objection.[355] However, when Plaintiffs filed their Complaint, incorporating their Objection, and alleged additional claims (including their own breach of contract claim) seeking the recovery of money, challenging the validity of Defendant's lien, and requesting an injunction, this proceeding became one under Rule 7001.[356] Pursuant

[350] ECF No. 23 at 24–25, ¶¶ 9–11, 17–19.
[351] *Id.* at 24, ¶¶ 7, 12.
[352] *Id.* at 24–25, ¶¶ 13, 20.
[353] ECF No. 36 at 8, ¶ 31.
[354] *Id.* at 7–8, ¶¶ 29–31.
[355] ECF No. 1.
[356] *See* FED. R. BANKR. P. 3007(b), 7003; *see also In re Simmons*, 765 F.2d at 552 ("The objection to a claim initiates a contested matter unless the objection is joined with a counterclaim asking for the kind of relief specified in Bankruptcy Rule 7001.").

to Rule 7001, Part VII of the Federal Rules of Bankruptcy, which includes Rule 7013, applies to adversary proceedings.

Moreover, as stated in COLLIERS, "[s]hould a counterclaim be based on one of the kinds of suits described in Rule 7001, the counterclaim must be asserted in the manner of a complaint to which the creditor would be obliged to interpose an answer."[357] Because Plaintiffs' Complaint brought claims fitting Rule 7001, Defendant was "obliged to interpose an answer." Plus, this Court ordered Defendant to submit an answer to Plaintiffs' Complaint.[358] Therefore, Defendant's Original Answer and Counterclaims[359] constitutes an answer,[360] wherein counterclaims are procedurally proper.

Lastly, Plaintiffs argue that Defendant's breach of contract counterclaim is not compulsory and arose pre-petition, so Defendant need not bring it now. Regardless whether the claim is not compulsory or arose pre-petition, Rule 7013, incorporating FRCP 13, permits a party to bring a non-compulsory pre-petition counterclaim in a responsive pleading.[361] Thus, Defendant's breach of contract counterclaim is procedurally proper as part of its answer.

b. Defendant's breach of contract claim is sufficiently pled

Plaintiffs move to dismiss Defendant's breach of contract claim arguing that Defendant did not sufficiently plead that Plaintiffs' alleged breaches were material. Plaintiffs also argue Defendant's damages allegation that "[a]s a result of Plaintiffs' defaults, [Defendant] has suffered actual

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[357] COLLIER ON BANKRUPTCY ¶ 502.02[3][b] (Richard Levin & Henry J. Sommer eds., 16th ed.); *see also In re Simmons*, 765 F.2d at 552.
[358] ECF No. 12.
[359] ECF No. 23.
[360] As stated *supra* in Part IV(A)(1)(a)(i), the portions of Plaintiffs' Complaint that incorporate Plaintiffs' Objection constitute an answer to Defendant's Claim No. 9-3. However, the remainder of Plaintiffs' Complaint is just that, a complaint, to which Defendant must file an answer.
[361] *See* FED. R. CIV. P. 13 ("A pleading may state as a counterclaim against an opposing party any claim that is not compulsory."); *see also* FED. R. BANKR. P. 7013 ("Fed. R. Civ. P. applies in adversary proceedings except that a party sued by a trustee or debtor in possession need not state as a counterclaim any claim that the party has against the debtor, the debtor's property, or the estate, unless the claim arose after the entry of an order for relief.").

damages," is a purely conclusory statement.[362] Under Texas law, the elements of a breach of contract claim are: (1) the existence of a valid contract; (2) performance or tendered performance by the plaintiff; (3) breach of the contract by the defendant; and (4) damages sustained by the plaintiff because of the breach.[363] Plaintiffs' contentions rest on the third and fourth elements.

Plaintiffs do not challenge the sufficiency of Defendant's allegations as to whether the Note or Deed of Trust were breached. Instead, Plaintiffs argue that Defendant needed to allege that the breach was material. However, the elements spelled out above contain no materiality requirement and Plaintiffs have not provided any legal authority for their contrary position. Plaintiffs' Motion to Dismiss conflates the elements of a breach of contract claim and the elements of an excuse for non-performance under a contract. The former contains no materiality requirement whereas the latter does. Questions of materiality arise when a party claims to be excused from performing under a contract because of the other party's prior material breach.[364] That was the exact issue raised in *Trevino*, erroneously cited by Plaintiffs in support of their argument. In *Trevino*, this Court considered materiality solely to determine whether the plaintiffs there were precluded from bringing a breach of contract claim against the defendant where the defendant alleged that the plaintiffs also breached the contract.[365] Nowhere did this Court say that materiality was a required element of the plaintiffs' breach of contract claim against the defendant.[366]

Moreover, to survive dismissal, Defendant must allege a "plausible, non-speculative claim for damages," but need not allege an exact dollar amount.[367] Here, Defendant alleges that it

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[362] ECF No. 36 at 6, ¶ 24 (citing ECF No. 23 at 4, ¶ 19).
[363] *Bridgmon v. Array Sys. Corp*., 325 F.3d 572, 577 (5th Cir. 2003).
[364] *Sky Capital Group, Ltd. v. Bombardier, Inc.*, 2014 Tex. App. LEXIS 12928, at *9 (Tex. App.—Dallas 2014, no pet.)
[365] *In re Trevino*, 535 B.R. at 155–56.
[366] *Id.*
[367] *See Harold H. Huggins Realty, Inc. v. FNC, Inc.*, 634 F.3d 787, 803 n.44 (5th Cir. 2011) (finding that simply pleading that the plaintiff lost business and profits due to the defendant's actions was sufficient in pleading damages); *see also Casares v. Agri-Placements Int'l, Inc.*, 12 F. Supp. 3d 956, 978 (S.D. Tex. Mar. 31, 2014) (collecting cases).

suffered actual damages because of Plaintiffs' failure to make timely payments, maintain insurance, and maintain the Property in a good and safe condition of repair.[368] Defendant also alleges that Plaintiffs have accrued $33,607.60 in arrearages.[369] Based on those allegations, it is plausible that Plaintiffs' alleged breaches caused actual damage to Defendant.

Accordingly, Plaintiffs' Motion to Dismiss Defendant's Counterclaim I is denied.

2. Defendant's Counterclaim II (declaratory judgment)

Defendant's Counterclaim II requests a judgment from this Court declaring that Defendant has a right to seek nonjudicial foreclosure against the Property.[370] Plaintiffs move to dismiss Defendant's Count II, arguing that Defendant has not pled facts from which this Court can plausibly determine that Defendant has cause for relief from the automatic stay, including either a lack of adequate protection or that Plaintiffs have no equity in the Property and the Property is not necessary for effective reorganization.[371] In response, Defendant cites *Campbell* for the proposition that the "automatic stay serves to protect the bankruptcy estate from actions taken by creditors outside the bankruptcy court forum, not legal actions taken within the bankruptcy court."[372] Subsequent to *Campbell*, the Fifth Circuit in *Cowin* explained that "[w]hile the language in *Campbell* could suggest a broad rule, the holding was narrow: the automatic stay does not bar the filing of proofs of claim in the debtor's bankruptcy case."[373]

Defendant has not pointed this Court to any authority that extends the language in *Campbell* to an adversary proceeding wherein a creditor seeks a declaratory judgment for nonjudicial foreclosure. Pursuant to § 362(a), the automatic stay applies to any "judicial . . . action or

[368] ECF No. 23 at 25.
[369] *Id.* at 24–25, ¶¶ 13, 20.
[370] *Id.* at 26, ¶ 22(g).
[371] *Id.* at 9–10, ¶ 36.
[372] ECF No. 40 at 8 (quoting *Campbell v. Countrywide Home Loans, Inc.*, 545 F.3d 348, 356 (5th Cir. 2008)).
[373] *Cowin v. Countrywide Home Loans, Inc. (In re Cowin)*, 864 F.3d 344, 352 (5th Cir. 2017).

proceeding against the debtor."[374] The Fifth Circuit in *Campbell* noted that several courts had found that the automatic stay does not bar actions that are expressly allowed under the Bankruptcy Code, such as filing a proof of claim.[375] Nonjudicial foreclosure is not expressly allowed under the Bankruptcy Code. Absent any legal authority to the contrary, Defendant must plead that relief from the automatic stay is warranted under § 362(d)(1) or (2). Defendant has not done so. Any motion for relief from the automatic stay must be filed in the main bankruptcy case pursuant to Federal Rule of Bankruptcy Procedure 4001 and Bankruptcy Local Rule 4001-1.

Accordingly, Defendant's Counterclaim II is dismissed.

Defendant's Response states, "to the extent the Court determines Plaintiffs should be entitled to any relief . . . [Defendant] respectfully requests the opportunity to amend its pleadings to cure any deficiencies."[376] Although the Federal Rules of Civil Procedure contain liberal amendment rules, the party requesting amendment must at least "set forth with particularity the grounds for the amendment and the relief sought."[377] As observed by the Fifth Circuit in *Dow Chemical*, "a bare request in an opposition to a motion to dismiss - without any indication of the particular grounds on which the amendment is sought, *cf.* Fed. R. Civ. P. 7(b) - does not constitute a motion within the contemplation of Rule 15(a)."[378]

In *Dow Chemical*, the plaintiff filed a motion to amend consisting of three sentences, unsupported by affidavits, a brief, or a proposed amended complaint.[379] The plaintiff's motion stated, "in the event that the dismissal is denied, plaintiff requests leave of Court to file amended pleadings adding additional plaintiffs and facts as allowed by law."[380] The Court found that while, in the

[374] 11 U.S.C. § 362(a).
[375] 545 F.3d at 356–57.
[376] ECF No. 40 at 12.
[377] *United States ex. Rel. Doe v. Dow Chem. Co.*, 343 F.3d 325, 331 (5th Cir. 2003).
[378] *Id.* (internal quotation marks and citations omitted).
[379] *Id.*
[380] *Id.*

loosest sense, the motion was a request to amend, it offered no grounds on which amendment should be permitted.[381] "The absence of any proposed amendments, compounded by the lack of grounds for such an amendment," the Court concluded, "justifies the district court's implicit denial of [the plaintiff's] motion to amend his complaint."[382] Defendant's Response here, just as the plaintiff's motion in *Dow Chemical*, contains no grounds for permitting amendment and no proposed amendment. Defendant fails to even mention the Federal Rule of Civil Procedure that would permit it to amend its Answer. Defendant merely requests to amend "to cure any deficiencies" and notes that the amendment is not intended "for the purposes of delay."[383]

Moreover, a court may deny leave to amend where an amendment would be futile.[384] An amendment is futile if the amended claim could not survive a motion to dismiss.[385] Here, a motion for relief from the automatic stay must be filed in the main bankruptcy case pursuant to Federal Rule of Bankruptcy Procedure 4001 and Bankruptcy Local Rule 4001-1. Thus, any amendment to Defendant's Answer in this adversary proceeding seeking relief from the automatic stay in the underlying bankruptcy case would not survive a motion to dismiss.

Accordingly, Defendant's request to amend its answer and counterclaims is denied.

C. Plaintiffs' Motion for Judgment on the Pleadings

Plaintiffs also seek judgment on the pleadings as to Defendant's Counterclaims I and II. Plaintiffs assert that Count I should be dismissed pursuant to FRCP 12(c) because Defendant has not shown that it is the holder of the Note and Deed of Trust.[386] Plaintiffs assert that Count II

[381] *Id.*
[382] *Id.*
[383] ECF No. 40 at 12.
[384] *In re Hollie*, 622 B.R. at 235 (citing *Foman v. Davis*, 371 U.S. 178, 182 (1962)).
[385] *Id.* (quotation marks omitted) (quoting *Rio Grande Royalty Co., Inc. v. Energy Transfer Partners, L.P.*, 620 F.3d 465, 468 (5th Cir. 2010)).
[386] *Id.* at 3, ¶ 6.

should likewise be dismissed because (a) Defendant has not obtained stay relief and (b) Defendant has not shown that it is the holder of the Note and Deed of Trust.[387]

FRCP 12(c), incorporated by Federal Rule of Bankruptcy Procedure 7012, provides, "[a]fter the pleadings are closed–but early enough not to delay trial–a party may move for judgment on the pleadings." An FRCP 12(c) motion "is designed to dispose of cases where the material facts are not in dispute and a judgment on the merits can be rendered by looking to the substance of the pleadings and any judicially noticed facts."[388] In determining whether Plaintiffs' FRCP 12(c) motion should be granted, this Court must view all well-pleaded facts as true and in the light most favorable to Defendant as non-movant.[389] Conclusory allegations will not be accepted.[390] Defendant's Counterclaims I and II will not be dismissed unless Defendant would not be entitled to relief under any set of facts or any possible theory that it could prove consistent with the allegations in its Answer.[391]

1. Defendant's Counterclaim I (breach of contract)

Plaintiffs move to dismiss Defendant's breach of contract claim on the ground that Defendant cannot enforce the Note and Deed of Trust against Plaintiffs because the pleadings do not show that Defendant is the legal holder of those documents.[392] Defendant responds that its Motion to Dismiss seeks to dismiss Plaintiffs' challenge to the lien on *res judicata* and judicial estoppel grounds and the 2010 Modification Agreement entered into by Defendant and Plaintiffs.

Plaintiffs' argument fails for several reasons. First, this Court already held that Plaintiffs are barred from challenging the validity of Defendant's lien for lack of standing and on *res judicata*

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[387] *Id*. at 3, ¶ 5.
[388] *Great Plains Trust Co. v. Morgan Stanley Dean Witter & Co.*, 313 F.3d 305, 312 (5th Cir. 2002) (quoting *Hebert Abstract Co. v. Touchstone Props., Ltd.*, 914 F.2d 74, 76 (5th Cir. 1990)).
[389] *Id.* at 312–13.
[390] *Id.* at 313.
[391] *Id.* (citing *Jones v. Greninger*, 188 F.3d 322, 324 (5th Cir. 1999)).
[392] ECF No. 36 at 12, ¶ 44.

grounds. Second, the assignments of the Note and Deed of Trust are facially valid, transferring interest in them to Defendant. The assignments reflect that the Note and Deed of Trust were first assigned by InterBay Funding, LLC, to Wachovia Bank, N.A. as Indenture Trustee (Bayview),[393] and then from Wachovia Bank, N.A. as Trustee (Bayview) by Its Attorney-in-Fact Bayview Loan Servicing, LLC, to Bayview Loan Servicing, LLC,[394] now known as Community, Defendant in this case. Third, Plaintiffs attached the 2010 Modification Agreement to their Complaint.[395] That agreement is between Defendant and Plaintiff Ramon Blanco as borrower and indicates that Defendant is the holder or the servicing agent of the holder of the Note executed by the borrower in 2001 in the amount of $68,000.[396] It also says that "the note evidences a loan . . . along with a Deed of Trust or Mortgage ("Security Instrument") securing said Note."[397] The Modification Agreement reflects that Defendant is the holder of the Note and Deed of Trust.

Additionally, in a footnote, Plaintiffs ask this Court to dismiss Defendant's breach of contract claim because "even if the Court finds that Defendant holds good title to the Note and Deed of Trust, the pleadings show that Defendant committed a prior material breach, and therefore cannot prevail on its breach of contract counterclaim."[398] Generally, a party in breach of contract cannot maintain a suit for breach against another contracting party.[399] If Defendant committed a material breach of the Note or Deed of Trust, then Plaintiffs were excused from any obligation to perform.[400] However, when one party breaches a contract, the other party is entitled to terminate

[393] ECF No. 21-5.
[394] ECF No. 21-7.
[395] ECF No. 21-6.
[396] *Id.* at 1.
[397] *Id.*
[398] ECF No. 36 at 12 n.4.
[399] *In re Trevino*, 535 B.R. at 155 (citations omitted); *see also* Romero *v. Ocwen Loan Serv., LLC*, 2018 U.S. Dist. LEXIS 218820, at *25–26 (quoting *Peters v. JP Morgan Chase Bank, N.A.*, 600 F. App'x 220, 224 (5th Cir. 2015)).
[400] *In re Trevino*, 535 B.R. at 155.

the contract and sue for breach, "[b]ut a party who elects to treat a contract as continuing deprives himself of any excuse for ceasing performance on his own part."[401]

Plaintiffs' Complaint alleges that Defendant committed a prior material breach of the Note and Deed of Trust by violating Rule 3002.1 three times between 2013 and 2015 and misapplying payments in violation of sections 2.1 and 2.4 of the Deed of Trust and the payment provisions of the Note.[402] But, as pointed out in Plaintiffs' Complaint and Defendant's Answer, Plaintiffs voluntarily stopped making payments under the Note in November 2018, years after Defendant allegedly breached the Note and Deed of Trust.[403] Thus, it is plausible that Plaintiffs deprived themselves of any excuse for ceasing to make payments by continuing to perform under the Note and Deed of Trust for several years after Defendant's alleged breach. Therefore, this Court cannot conclude that there is no set of facts or any possible theory that Defendant could prove consistent with the allegations in its answer that would entitle it to relief for breach of contract.

Accordingly, Plaintiffs' FRCP 12(c) motion to dismiss Defendant's Counterclaim I is denied.

2. Defendant's Counterclaim II (declaratory judgment)

Plaintiffs move under FRCP 12(c) to dismiss Defendant's Counterclaim II on two grounds: (1) that Defendant has not alleged facts showing that it is entitled to relief from the automatic stay and (2) that Defendant has not sufficiently pled that it is the holder of the Note and Deed of Trust. For the reasons explained above, Plaintiffs' request for dismissal of Defendant's Counterclaim II on the ground that Defendant is not the legal holder of the Note and Deed of Trust is denied.

[401] *Long Trusts v. Griffin*, 222 S.W.3d 412, 415 (Tex. 2006). (cleaned up) (quoting *Hanks v. GAB Bus. Servs., Inc.*, 644 S.W.2d 707, 708 (Tex. 1982)).
[402] ECF No. 21 at 17–18, 34–35, ¶¶ 81, 170–71.
[403] *Id.* 15–16, ¶ 21; ECF No. 23 at 24, ¶ 9.

Furthermore, this Court has already found that Defendant's request for declaratory judgment is dismissed under FRCP 12(b)(6).

Accordingly, Plaintiffs' FRCP 12(c) motion to dismiss Defendant's Counterclaim II is denied as moot. Defendant's Count II is dismissed pursuant to Federal Rule of Civil Procedure 12(b)(6) as stated *supra*.

V. CONCLUSION

An order consistent with this Memorandum Opinion will be entered on the docket simultaneously herewith.

SIGNED September 14, 2021

Eduardo Rodriguez
United States Bankruptcy Judge

Faculty

Theodore O. Bartholow, III is a partner with Kellett & Bartholow PLLC in Dallas, where he focuses on representing consumers from around the country in individual and class-action litigation against financial services providers and related entities, including mortgage-servicers, debt-collectors and other consumer creditors, with a focus on matters arising in and related to consumer bankruptcy. He also has substantial experience representing consumer creditors in connection with chapter 11 bankruptcies filed by consumer lenders and mortgage-servicers, including active roles in the recent Think Finance (N.D. Tex.) and Ditech (S.D.N.Y.) bankruptcies, in which he was particularly active on behalf of his consumer clients. Mr. Bartholow is a member of the John C. Ford American Inn of Court, received the National Association of Consumer Bankruptcy Attorneys' Distinguished Service Award in 2016, and represented the National Association of Consumer Bankruptcy Attorneys at a "Mortgage Mini-Conference" focusing on development of Bankruptcy Rule 3002.1 held by the Rules Committee of the National Conference of Bankruptcy Judges in 2012. His written work has been published in the *ABI Journal*, among other publications, and he has spoken at ABI conferences and at numerous other national conferences, including the National Conference of Bankruptcy Judges Annual Conference (2017), the National Consumer Law Center's Consumer Rights Litigation Conference (2016, 2020), the National Association of Consumer Advocates and the National Association of Consumer Bankruptcy Attorneys, in addition to frequent presentations at local and regional continuing legal education events and webinars. In connection with representation of his consumer clients, Mr. Bartholow has been quoted by "NBC News," *The New York Times*, *The Wall Street Journal*, *The Los Angeles Times*, *The Chicago Tribune*, *The Dallas Morning News*, *ProPublica* and "CNN Money," among others. He received his undergraduate degree in philosophy from the University of Texas in 1998 and his J.D. in 2002 from the Benjamin N. Cardozo School of Law in New York, where he was executive editor of the *Cardozo Journal of International and Comparative Law*.

O. Max Gardner is a consumer bankruptcy attorney with Max Gardner Law PLLC in Shelby, N.C., and his work against predatory lenders and mortgage servicers has been featured in ABC News's "Nightline," PBS's "Frontline," CNN, *BusinessWeek*, *The New York Times*, *The Washington Post*, *Forbes* and many other news outlets across the country. He has also taken the lead in pursuing the attempts of many creditors to collect debts legally discharged in bankruptcy cases, and has trained hundreds of lawyers at his "Consumer Bankruptcy Boot Camps" for many years. The National Association of Consumer Bankruptcy Lawyers (NACBA) named Mr. Gardner a Champion of Consumer Rights in 2003, named him the Outstanding Consumer Lawyer of 2004 and awarded him The Distinguished Service Award in April 2013. Mr. Gardner was elected a member of the North Carolina Legal Elite by *Business North Carolina* from 2004-07. He was also recognized as a "Super Lawyer" in North Carolina by *Charlotte Magazine* and by *Law & Politics* from 2006-10 in the field of Consumer Bankruptcy Law, and is rated AV-Preeminent by Martindale-Hubbell. Previously, Mr. Gardner was a senior law clerk to Hon. William H. Bobbitt, the late Chief Justice of the North Carolina Supreme Court, and to Hon. William Copeland, an Associate Justice of that court. He also worked as an associate with the law firm of Smith, Moore, Smith, Schell & Hunter until 1977, when he opened a consumer-based law practice in Shelby, N.C. In addition, he served as treasurer for McNeill Smith's 1978 Campaign for the U.S. Senate, was Of Counsel for Sims, Walker & Steinfeld of Washington, D.C., from 1983-94, and served as general counsel to the Democratic Party of North

Carolina from 1993-97. Mr. Gardner is a member of the North Carolina State Bar, North Carolina Bar Association, North Carolina Academy of Trial Lawyers, American Bar Association, American Bar Institute, American Trial Lawyers Association, National Association of Criminal Defense Lawyers, Southern Trial Lawyers Association, National Association of Consumer Bankruptcy Attorneys, National Association of Consumer Advocates, National Association of Chapter 13 Trustees, Civil Justice Foundation, National Consumer Law Center, Cleveland County Bar Association and 27-B Judicial District Bar Association. He received his undergraduate degree from the University of North Carolina at Chapel Hill in 1969 and his J.D. with high honors from the UNC School of Law in 1974, where he was a member of the *North Carolina Law Review*, president of the Student Bar Foundation, named the Outstanding Law School Graduate of 1974 and elected to the Order of the Coif.

Glenn E. Glover is a partner with Bradley Arant Boult Cummings LLP in Birmingham, Ala., and has a broad practice that includes representing creditors in out-of-court workouts, bankruptcy cases and a variety of litigation settings. He also has experience in representing mortgage-servicers and other financial institutions in mortgage-related litigation in bankruptcy courts. Mr. Glover has practiced in the area of bankruptcy and creditors' rights for over 14 years. His practice involves a significant amount of workouts and restructurings for banks and other financial institutions, spanning both the transactional and litigation areas of the law. He has experience in real estate workouts of all sizes. Mr. Glover is particularly familiar with important issues associated with drafting and securing favorable forbearance and modification terms for his clients with distressed loans, in addition to the numerous tools that are available for his clients' use and advantage. On the litigation side, he follows his clients' distressed loans into bankruptcy or litigation whenever necessary, and has taken scores of depositions and handled numerous evidentiary hearings in both federal and bankruptcy courts for his clients. Mr. Glover has experience with a variety of creditor arrangements, from simple notes payable to syndication deals, and has obtained numerous successes in his practice by assisting his creditor clients in obtaining payment in full and defeating lender-liability claims raised by borrowers. He also has experience in representing mortgage-servicing clients in litigation in bankruptcy courts and is familiar with the numerous types of bankruptcy and nonbankruptcy claims brought against mortgage-servicers in litigation, including discharge violations, violations of the automatic stay, violations of confirmation orders, and violations of numerous other bankruptcy statutes and rules. In addition, he is knowledgeable of nonbankruptcy claims, including FCRA, FDCPA, RESPA and TILA allegations. Mr. Glover received his B.A. *magna cum laude* and Phi Beta Kappa in 1992 from the University of Alabama, his M.A. in 1995 from the University of Alabama at Huntsville, his M.A. in 1996 from the University of Alabama at Birmingham, and his J.D. *cum laude* in 2000 from the University of Alabama School of Law.

Hon. Jennifer H. Henderson is a U.S. Bankruptcy Judge for the Northern District of Alabama in Tuscaloosa, sworn in on Feb. 16, 2015. Previously, she was a partner with Bradley Arant Boult Cummings LLP's Bankruptcy, Restructuring and Distressed Investing Practice Group in Birmingham, Ala., where she represented debtors and creditors in bankruptcy cases, out-of-court workouts and restructurings and bankruptcy- related litigation. Judge Henderson clerked for Hon. Thomas B. Bennet and is listed as a 2014 Alabama Super Lawyers "Rising Star." She received her B.A. *magna cum laude* from Birmingham-Southern College in 2001 and her J.D. *summa cum laude* form the University of Alabama School of Law in 2004, where she was a member of the Order of the Coif and a special works editor for the *Alabama Law Review*.