

Can a Creditor Violate the Automatic Stay in Bankruptcy by Doing Nothing?

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Filing a bankruptcy petition automatically halts efforts to collect pre-petition debts from the debtor outside of bankruptcy.

If a creditor wants to continue a lawsuit against a debtor outside of bankruptcy, repossess collateral, terminate a lease, set off debts, or pursue other collection efforts, it

first must obtain stay relief from the bankruptcy court. The "automatic stay" is a command to halt action, and creditors violate it at their own peril.

But what about inaction? If a creditor began collection activity before the bankruptcy, must it unwind its actions when notified of the filing? Can a creditor violate the automatic stay by doing nothing? A recent decision by a bankruptcy court in Virginia says "yes," but other courts have said "no." The United States Supreme Court is likely to resolve the uncertainty this summer. Meanwhile, creditors may want to err on the side of caution.

Attorney Griffin represented Randi Nimitz in her divorce before she filed for bankruptcy. Griffin did not pay all her legal fees, and Griffin obtained a judgment against her for \$10,000. Virginia allows wage garnishment, so Griffin obtained a garnishment order against Nimitz. The state court was holding \$1,000 in wage deductions, and a hearing on turning over the funds to Griffin was scheduled when Nimitz filed Chapter 7. Her bankruptcy petition listed Griffin's judgment as debt and claimed an exemption in the \$1,000. Nimitz's counsel notified Griffin and demanded he terminates the garnishment. Griffin refused. He claimed that he could do nothing because he had no legal obligation to take affirmative action to terminate the garnishment.

Nimitz moved for Griffin to be held in contempt for a willful violation of the automatic stay. The bankruptcy court agreed. To prove a stay violation, a party must establish that (1) a violation occurred, the violation was committed willfully, and (3) the violation caused actual damages. The automatic stay prohibits any act to obtain possession of property of the estate or to exercise control over estate property. The bankruptcy court reasoned that property seized pre-petition, but not yet liquidated, remains property of the bankruptcy estate. The debtor's bankruptcy estate includes a possessory interest in property not held at the time of filing.

The bankruptcy court concluded that Griffin's refusal to terminate the garnishment amounted to the improper exercise of control over the debtor's property. Griffin did not assert an ownership interest or lien in the garnished funds, which did not help his argument. The bankruptcy court awarded Nimitz attorneys' fees of

\$2,400 to prosecute the contempt motion.

The United States Supreme Court should rule definitively on this issue sometime this summer. It is possible they will rule that mere inaction does not violate the automatic stay. But unless that happens, creditors who fail to unwind collection efforts when demanded to do so by a debtor in bankruptcy risk being held in contempt and liable for damages.

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