Dischargeability of Criminal Restitution in Bankruptcy in the 10th Circuit

While bankruptcy is a valuable tool for eliminating debt acquired from a variety of sources, the Bankruptcy Code prohibits the discharge of certain debts, including an obligation for restitution entered after a criminal conviction.

The 10th Circuit Bankruptcy Appellate Panel (the "Panel") recently issued an opinion in *In Re Paul Chayne Williams*, BAP No. CO-10-020, that squarely addresses this issue and articulates the reasons for the prohibition.

Debtor and Appellant Paul Chayne Williams ("Williams") sued Appellees Donald H. and Suzanne S. Meyers (the "Meyers"), claiming that the Meyers had violated the discharge injunction by obtaining a restitution order against Meyers and seeking a declaratory order that his restitution obligation had been discharged in his bankruptcy case filed before the restitution order entered.

Williams' complaint alleged that the Meyers had improperly sought to collect a discharged debt by pursuing criminal prosecution against him for securities fraud. In 1997, Williams had borrowed money from Mr. Meyer. Later that year, Williams filed bankruptcy and the loan was discharged. Later, after the Meyers went to the district attorney to report what they believed was Williams' fraudulent activity. What Williams characterized as a loan, the district attorney characterized as "fraud and other prohibited conduct in the offer and sale of a security". Williams was eventually convicted for securities fraud, and not just for the transaction with the Meyers. As part of his punishment, Williams was ordered to pay restitution.

Williams appealed the bankruptcy court's order dismissing his complaint against the Meyers for failing to state a claim for which relief may be granted. The 10th Circuit Bankruptcy Appellate Panel took up Williams' appeal and published its opinion on November 9, 2010.

At the outset of its opinion, the Panel notes that a bankruptcy discharge "voids any judgment at any time obtained, to the extent that such judgment is a determination of the personal liability of the debtor with respect to any debt discharged under section 727 [of the Bankruptcy Code]" and that the discharge also "operates as an injunction against the commencement or continuation of an action, the employment of process, or an act to collect, recover, or offset any such debt as a personal liability of the debtor."

The Panel then continues its analysis by pointing to the section of the Bankruptcy Code, §523(a)(7), which provides that a discharge does not discharge any debt "to the extent such debt is for a fine, penalty, or forfeiture payable to and for the benefit of a governmental unit, and is not compensation for actual pecuniary loss." 523(a)(7) is self-executing and does not require a party to obtain a judgment that the restitution debt is excepted from discharge. The party, usually a governmental entity, does not need to object to discharge in the case of criminal restitution obligations.

Requiring a governmental entity to appear in bankruptcy court to seek an exception to discharge would be "burdensome, duplicative, and unseemly." Further, excepting restitution orders would "hamper the flexibility of state criminal judges in choosing the combination of

imprisonment, fines, and restitution most like to further the rehabilitative and deterrent goals of state criminal justice systems."

Excepting restitution obligations from bankruptcy discharge is a common-sense answer to the question of whether someone should be able to wipe out punishment for a conviction of a criminal offense. Citing the U.S. Supreme Court, the Panel writes, "Unlike an obligation which arises out of a contractual, statutory or common law duty, here the obligation is rooted in the traditional responsibility of a state to protect its citizens by enforcing its criminal statutes and to rehabilitate an offender by imposing a criminal sanction intended for that purpose."

While Williams tries to distinguish his case by arguing that the Meyers pursued prosecution *after* his bankruptcy discharge had entered, the Panel is not swayed. Again, citing the U.S. Supreme Court, the Panel writes, "it does not matter whether a prepetition crime is discovered before or after the criminal defendant files bankruptcy." Again, this is a common sense solution to those who would try to absolve themselves from any pecuniary punishment by filing bankruptcy.

The Panel affirms the bankruptcy court's dismissal of Williams' complaint against the Meyers. As can be read in its opinion excluding a restitution obligation from bankruptcy discharge is an essential part of both the bankruptcy and criminal justice system.

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