

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF MISSISSIPPI

IN RE: JAMES A CARRUTH and
JUDITH E. CARRUTH
Debtors

CASE NO . 05-14774
CHAPTER 7

OPINION

On consideration before the court is a motion for sanctions filed by Manufacturers and Traders Trust Company (“MTTC”); a response thereto having been filed on behalf of the debtors and their counsel; and the court, having heard and considered same, hereby finds as follows;

to-wit:

I.

The court has jurisdiction of the parties to and the subject matter of this contested proceeding pursuant to 28 U.S.C. §1334 and 28 U.S.C. §157. This is a core proceeding as defined in 28 U.S.C. §157(b)(2)(A), (B) and (O).

II.

Subsequent to the two hearings conducted on MTTC’s motion for sanctions, the debtors’ attorney passed away unexpectedly. The court made inquiry of MTTC’s counsel as to whether MTTC still desired to prosecute the motion for sanctions considering this event. MTTC indicated that it wanted a final decision from the court which is clearly its prerogative.

III.

On December 6, 2002, the debtors commenced a civil cause of action in the Circuit Court of the First Judicial District of Hinds County, Mississippi, against MTTC and numerous other parties, including several principals of Southern Mortgage Company (“Southern Mortgage”). The suit was not filed directly against Southern Mortgage which apparently had filed a

bankruptcy case in the State of Louisiana. In their complaint, the debtors sought monetary damages against the non-MTTC defendants and further sought to void or rescind a promissory note and deed of trust held by MTTC, based on the alleged misconduct of the aforementioned principals of Southern Mortgage, as well as, its agents.

Southern Mortgage originated the subject loan and held the note and deed of trust at the time of the alleged wrongdoing. Debtors' counsel admitted that MTTC took no part in any of the alleged wrongdoing, as well as, that the debtors had no valid monetary damage claim against MTTC.

IV.

On August 19, 2005, the debtors commenced Adversary Proceeding No. 05-1196 in this court against MTTC and Southern Mortgage. The complaint recited the same facts and circumstances that were pled in the state court cause of action and asserted the identical claim with respect to voiding or rescinding MTTC's note and deed of trust.

V.

On October 11, 2005, MTTC removed the state court cause of action to the United States District Court for the Southern District of Mississippi. It was transferred to the United States District Court for the Northern District of Mississippi and referred to this court by agreement on January 20, 2006. It was assigned Adversary Proceeding No. 06-1119. On June 2, 2006, the removed state court proceeding was consolidated into the pending adversary proceeding under Adversary Proceeding No. 05-1196.

VI.

At the time the debtors filed the adversary proceeding in this court on August 19, 2005, they no longer had any ownership interest in the real property which was encumbered by the deed of trust held by MTTC. The debtors had conveyed title to this property even before filing bankruptcy to Mortgage Financing, Inc., (“MFI”), an entity solely owned by the spouse of debtors’ counsel. The debtors’ bankruptcy schedules evidenced this occurrence by indicating that the debtors owned no real property, as well as, by reflecting that MTTC had only an unsecured, non-priority claim against the bankruptcy estate.

Based on the debtors’ conveyance of title to MFI, MTTC asserted in its answer and affirmative defenses to the adversary proceeding complaint, which it filed on October 11, 2005, that the debtors lacked standing to prosecute the adversary proceeding. Debtors’ counsel never disputed the validity of this defense. Indeed, he admitted in a letter to the court, dated August 25, 2006, a copy of which was served on MTTC’s counsel, that the avoidance claim asserted by the debtors against MTTC was not valid as a result of the debtors’ lack of ownership of the property. Specifically, his letter stated the following:

In the ’05 adversary, the Plaintiffs sought damages/recoupment against Southern as a parry [sic] to the note held by Manufacturers & Traders and in defense of enforcement of the mortgage. Manufacturers & Traders answered that the Plaintiffs no longer had standing because they had sold the property. Considering that defense, I believed it valid. The Plaintiffs had no direct claim against Manufacturers & Traders for predatory lending as it was a subsequent assignee, though maybe it had some notice of the acts of Southern and/or ContiMortgage, Southern’s assignee. Notice would address enforcement of the mortgage but not subject Manufacturers & Traders to damages.

Because MTTC did not press to dismiss the adversary proceeding by requesting a hearing to address the affirmative defense that it had previously pled, debtors’ counsel continued to pursue the adversary proceeding against both MTTC and Southern Mortgage. On November 7,

2005, debtors' counsel filed an application for the entry of default against Southern Mortgage, coupled with a motion for a judgment by default, and a proposed judgment by default. The form of the judgment by default even purported to void MTTC's note and deed of trust. MTTC filed a response objecting to the entry of the proposed default judgment, and a hearing on these pleadings was scheduled on December 14, 2005. As a result of that hearing, the court entered a default judgment against Southern Mortgage in the debtors' favor, but fully implemented the safeguards requested by MTTC in its response.

On December 29, 2005, ten (10) days after this court entered the default judgment against Southern Mortgage, debtors' counsel filed a motion to voluntarily dismiss the adversary proceeding. A telephonic status conference addressing this motion was conducted on March 9, 2006, during which debtors' counsel decided to withdraw the motion to dismiss and to continue to pursue the claim against MTTC.

On September 29, 2006, the court held a telephonic hearing necessitated by two concerns:

(1) Debtors' counsel had failed to timely submit an acceptable order withdrawing the motion to dismiss, and (2) Debtors' counsel had alternatively submitted an order for the voluntary dismissal of the consolidated adversary proceeding "without prejudice." At this hearing, the debtors' lack of standing was raised and the court concluded that the debtors no longer had an avoidance or rescission claim against MTTC. Accordingly, the consolidated adversary proceeding was dismissed "with prejudice" at the cost of the debtors by an order entered on October 27, 2006.

VII.

In light of the above facts and procedural history, the court finds that debtors' counsel initiated the adversary proceeding in this court without a justifiable legal basis. As such, the court finds that the conduct of the debtors' counsel warrants the imposition of sanctions pursuant to Rule 9011, Federal Rules of Bankruptcy Procedure, as well as, the inherent powers of this court. See, *In re Bryson*, 131 F.3d 601(7th Cir. 1997); *In re Clark*, 223 F.3d 859 (8th Cir. 2000); *In re Case*, 937 F.2d 1014 (5th Cir. 1991); *In re Weaver*, 307 B.R. 834 (Bankr. S.D. Miss. 2002); *Chambers v. NASCO, Inc.*, 501 U.S. 32 (1991); *NASCO v. Calcasieu Television and Radio, Inc.*, 894 F.2d 696 (5th Cir. 1990); and *In re Jefferson*, 59 B.R. 707 (Bankr. S.D. Miss. 1986).

VIII.

The motion for sanctions filed by MTTC seeks attorney fees and expenses both from the debtors and debtors' counsel. Evidenced by an itemization, requested by the court, MTTC seeks attorney fees in the sum of \$58,318.18, and expenses in the sum of \$1,762.95. Having carefully considered what could and should have happened in this proceeding, the court finds that the amount of attorney fees requested by MTTC should be reduced significantly.

As noted hereinabove, the debtors had transferred their interest in the subject real property to MFI prior to filing their bankruptcy case, as well as, prior to initiating the initial adversary proceeding in this court. According to the time records submitted by MTTC's counsel: a proceeding file was opened on September 6, 2005; a motion to dismiss was discussed by MTTC's counsel within a week of opening the file; the standing issue was raised within three weeks; and MTTC's counsel discussed this issue with debtors' counsel in a telephonic

conference on September 22, 2005. MTTC asserted on October 11, 2005, in its answer and affirmative defenses to the debtors' complaint, that the debtors lacked standing to prosecute a claim against MTTC. Not only was the validity of this defense never disputed by the debtors' counsel, he acknowledged the validity of the defense in the letter to the court mentioned hereinabove. As such, the court is of the opinion that MTTC clearly had knowledge of the debtors' lack of standing and could have pressed for a dismissal of the proceeding within a matter of weeks after filing its answer. Neither a motion for summary judgment nor a Rule 12(b)(6) motion to dismiss was ever filed in the adversary proceeding on behalf of MTTC. A successful outcome was very predictable.

The imposition of sanctions is not warranted for any events that occurred before the adversary proceeding was filed in this court or before the debtors conveyed their real property to MFI. (The debtors' cause of action against MTTC was potentially viable jurisdictionally prior to the transfer.) The adversary proceeding's history in this court extended for slightly more than 14 months. This is certainly not an excessive period of time, but as noted above, this history should have been significantly less. There was no need to incur attorney fees amounting to \$58,318.18, and this court refuses to sanction debtors' counsel for work that could have been avoided. However, the court will impose sanctions on debtors' counsel for the fees and expenses that were reasonably and necessarily incurred on behalf of MTTC in actually getting the proceeding dismissed because of the debtors' lack of standing. In this limited context, the court calculates the allowed attorney fees and expenses for MTTC as follows:

William H. Leech -	10.5 hours @ \$250.00 per hour	\$2,625.00
Danny Rule -	.5 hours @ \$175.00 per hour	87.50
S. Schelver (paralegal) -	2.0 hours @ \$110.00 per hour	220.00
Total Expenses Allowed		<u>1,355.95</u>
Total		\$4,288.45

The motion for sanctions filed by MTTC is granted in part. Sanctions are imposed against the debtors' counsel, R. Charles Robb, for attorney fees and expenses, set forth hereinabove, in the total sum of \$4,288.45. The court declines to impose sanctions against the debtors who had little, if nothing, to do with the proceedings filed and prosecuted in this court. A separate judgment shall be entered contemporaneously herewith in the aforesaid amount upon which interest may accrue from the date of the entry at the highest rate according to law.

ORDERED and ADJUDGED this the 31st day of August, 2007.

/s/ David W. Houston, III
 DAVID W. HOUSTON, III
 UNITED STATES BANKRUPTCY JUDGE