BEFORE THE TENNESSEE REGULATORY AUTHORITY
AT NASHVILLE, TENNESSEE

IN RE:	)	
	)	DOCKET NO. 98-00018
SHOW CAUSE PROCEEDING AGAINST	)	
MINIMUM RATE PRICING, INC.	)	

BRIEF ON JURISDICTIONAL ISSUE

Comes the Consumer Advocate Division (CAD) of the Office of the Attorney General in accordance with the April 6, 1999 oral decision of the agency and the April 7, 1999 Notice to file this brief on the question "whether the Tennessee Regulatory Authority retains jurisdiction to commence or continue with rendering a decision in an action or proceeding to enforce its police and regulatory power after the taking of evidence when the subject of the evidentiary proceeding files for bankruptcy under federal law before the decision is rendered?" CAD concludes that the Tennessee Regulatory Authority has authority to commence with or continue to a decision in the exercise of its police and regulatory decision because the bankruptcy Act, 11 U.S.C. § 362 (b) (4) expressly provides that a governmental agency is exempt from the automatic stay provisions of the bankruptcy act when it is exercising its police power. Moreover, CAD concludes that the Federal Bankruptcy Code is unconstitutional to the extent it could be applied to the Tennessee Regulatory Authority or the State of Tennessee so long as the Attorney General and the Tennessee Regulatory Authority do not waive Eleventh Amendment Sovereign Immunity by filing a proof of claim in bankruptcy Court.

Summary of the Proceedings

On July 27, 1998 the Authority entered an Order pursuant to Tenn. Code Ann. § 65-2-106 requiring MRP to appear and show cause why a cease and desist order, penalty and/or Order revoking MRP's authority to provide telecommunications services in Tennessee should not be issued. The Directors also appointed a Hearing Officer to take such action as was necessary to facilitate the orderly and efficient hearing of the matters by the Authority. On September 3, 1998, the Executive Secretary of the Authority issued a Notice, pursuant to Tenn. Code Ann. § 4-5-306, for a Pre-hearing Conference on September 17, 1998, to: determine a statement of issues, obtain admissions of facts and documents in an effort to avoid unnecessary proof, establish witnesses as appropriate, establish a procedural schedule for the discovery of additional matters relevant to the allegations against MRP, and for such other purposes allowed by law.

Without prior or contemporaneous explanation, MRP failed to appear at the September 17, 1998 Pre-hearing Conference. The Hearing Officer proceeded to conduct the September 17, 1998 Pre-Hearing Conference without the participation of MRP, pursuant to Tenn. Code Ann. § 4-5-309(a), having due regard for the interest of justice and the orderly and prompt conduct of the proceedings.[1] MRP also failed to reply to the Authority's Order requiring MRP to appear and show cause. The Hearing Officer determined that MRP should be compelled by Order to file a written answer in response to the allegations presented in the July 27, 1998, Order, no later than September 24, 1998. Formal Hearings were conducted on November 24-25, 1998 and

[1] The record reflects that MRP has a pattern of failing or refusing to appear before regulatory bodies or ignores the regulatory body even when its certification is at issue. See orders of Nebraska, Wisconsin, and the Federal Communications Commission.

December 10-11, 1998. On February 2, 1999 post hearing briefs were submitted and on February 26, 1999 proposed findings of fact and conclusions of law were submitted.

On or about February 26, 1999, MRP apparently filed a petition for Chapter 11 bankruptcy in the Bankruptcy Court of New Jersey. Chapter 11 bankruptcies permit a company to reorganize.

Facts

CAD and the Tennessee Regulatory Authority staff argue that MRP has acquired the accounts of Tennessee consumers through fraud and misrepresentation in violation of statutes, rules or orders of the State of Tennessee and the Tennessee Regulatory Authority, including but not limited to, the unlawful switching and billing of services. We argue that MRP, in fact, further designed its tariffs so that consumers could not be switched from it upon the consumers discovery of the fraud. For a more extensive statement, CAD adopts its proposed findings of fact and conclusions of law for much of the factual portion of this brief and incorporates said facts herein by reference.[2]

As additional facts to be considered in weighing the veracity of MRP, CAD cites the attachment to the April 2, 1999 letter of Sara Colley, of the law firm Rubin, Winston, Dierks Harris & Cooks, to K. David Waddell of the Tennessee Regulatory Authority. Said Attachment A is purportedly a copy of a document from the Bankruptcy Court of New Jersey which shows that MRP has filed for bankruptcy and has no employees. If MRP has no employees it does not have anything it can reorganize. The company is simply attempting to use the courts as a shield

[2]A copy of CAD's proposed findings of fact is attached to this brief.

to continue its unlawful actions.

CAD further submits a copy of a March 26, 1999 Attachment B letter from Eric M. Rubin of the law firm Rubin, Winston, Dierks Harris & Cooks, to Dorothy Attwood of the Federal Communications Commission, on behalf of MRP. Said March 26, 1999 letter is relevant because it demonstrates that MRP, the company charged with fraudulent violations of the statutes rules or orders of Tennessee, is continuing to engage in marketing services *despite the fact that it has no employees*. These services allegedly include operator response, account administration and marketing services. See March 26, 1999 letter from Rubin to Attwood.

Moreover, the March 26, 1999 letter demonstrates that MRP has testified falsely in this proceeding regarding its parent company and its relationship with Flat Rate Long Distance. In proceedings before this agency MRP represented that its parent company is "Parcel Consultants." (See Attachment C Tr. Vol.II, p.323 testimony of Drew Keena). MRP also failed to disclose the existence of Flat Rate Long Distance. (See Attachment D Tr. Vol. III p. 683 testimony of Drew Keena). In addition MRP also failed to disclose that it had other business plans. (See Attachment E Tr. Vol. II, p.340-350 testimony of Drew Keena). The information contained in the March 26, 1999 letter and the attachment to the prior letter demonstrates that representations of MRP are not trustworthy.

An additional fact for consideration is MRP's sale of its accounts to OAN. If the TRA fails or refuses to decide whether or not MRP violated statutes, rules or orders of the State of Tennessee and revoke its certificate, OAN will simply continue the unlawful billing and collection. (See Attachment F, Order of the Bankruptcy Court). If the TRA finds that MRP has in fact violated statutes, rules, or orders, the billing and collection will not occur and OAN has

recourse through its contract with MRP. Consumers will have no recourse.

Moreover, consumers will not be able to establish a right to payment if the TRA fails to adjudicate the slamming and cramming issues. (See In re: Taibbi, 213 B.R. 261 (E.D. N.Y., 1997).

ARGUMENT

A. The State of Tennessee is entitled to Sovereign Immunity.

The Eleventh Amendment to the U.S. Constitution provides:

> The Judicial power of the United States shall not be construed to extend to any suit in law or equity, commenced or prosecuted against one of the United States by Citizens of another State, or by Citizens or Subjects of any Foreign State.

The purpose of the Eleventh Amendment was to prevent the indignity of subjecting a State to the coercive process of judicial tribunals at the instance of private parties. Puerto Rico Aqueduct v. Metcalf & Eddy, 506 U.S. 139, 146, 113 S.Ct. 684, 688-89, 121 L.Ed.2d 605 (1993); In re Martinez, 196 B.R. 225, 228 (D. Puerto Rico 1996). Moreover, the Eleventh Amendment restricts the judicial power under Article III, and an Article I exercise of power, such as the Bankruptcy Code, cannot be used to circumvent the constitutional limitations placed upon federal jurisdiction; therefore the Bankruptcy Code, as it purports to apply to governmental units of State governments is an unconstitutional violation of States' right to Sovereign Immunity. In re Martinez, 196 B.R. at 230. See also, In re Fernandez, Civ. A. No. 97-0083, (U.S.D.C.-E.D. LA. 1997) (reversing decision of Bankruptcy Court as it affect the State of Louisiana, Department of Transportation); Koehler v. Iowa College Student Aid Commission, 204 B.R. 210 (B.C.-D. Minnesota 1997); In re York-Hannover Developments v. State of Florida Department of Revenue, 201 B.R. 137 (B.C.-N.C. 1996).

B. The Tennessee Regulatory Authority exercise of police or regulatory power is excepted from the automatic stay under prior law.

Even if the Eleventh Amendment did not apply the TRA would have power to act until a stay was invoked by the Bankruptcy Court. The United States Code, 11 U.S.C. § 362 provided in relevant part:

> Automatic stay
> (a) **Except as provided in subsection (b) of this section, a petition** filed under section 301, 302, or 303 of this title, or an application filed under section 5(a)(3) of the Securities Investor Protection Act of 1970, **operates as a stay, applicable to all entities**, of--
>
> (1) the commencement or continuation, including the issuance or employment of process, of a judicial, administrative, or other action or proceeding against the debtor that was or could have been commenced before the commencement of the case under this title, or to recover a claim against the debtor that arose before the commencement of the case under this title;
>
> (3) any act to obtain possession of property of the estate or of property from the estate or to exercise control over property of the estate...
>
> (b) **The filing of a petition under section 301, 302, or 303 of this title**, or of an application under section 5(a)(3) of the Securities Investor Protection Act of 1970, **does not operate as a stay--**
>
> (1) under subsection (a) of this section, of the commencement or continuation of a criminal action or proceeding against the debtor;
>
> (4) under subsection (a)(1) of this section, **of the commencement or continuation of an action or proceeding by a governmental unit to enforce such governmental unit's police or regulatory power**;
>
> (5) under subsection (a)(2) of this section, **of the enforcement of a judgment, other than a money judgment, obtained in an action or proceeding by a governmental unit to enforce such governmental unit's police or regulatory power**;

In most cases the filing of a petition or "application" pursuant to subsection (a) operates as a stay and no action is required by the Bankruptcy Court. But the filing of a petition does not operate as a stay when a governmental unit's police or regulatory power has been invoked to "enforce" something other than a monetary judgment in accordance with subsections (b) (4) and (b) (5). Javens v. City of Hazel Park, 107 F.3d 359, 363 (Sixth Cir. 1997). Furthermore, the governmental unit is not required to seek a determination by the Bankruptcy Court that its exercise of power is in fact of a police or regulatory origin. Javens v. City of Hazel Park, 107 F.3d at 365-66, citing Board of Governors of The Federal Reserve System v. MCorp Financial, 502 Us. 32, 112 S.Ct. 459, 116 L.Ed.2d 358 (1991).

In Yellow Cab Cooperative v. Metro Taxi,, for example, the Court of Appeals affirmed the District Court's reversal of a Bankruptcy Court's order enjoining the Colorado Public Utilities Commission's restriction on the debtor's operating certificate. 132 F.3d 591 (Tenth Cir. 1997). The Court of Appeals held that the automatic stay was not applicable despite the fact that the utilities commission was exercising control over the estate as contemplated by 11 U.S.C. 362 (a) (3) and the exceptions for police and regulatory power on their face applied only to subsections (a) (1) and (a) (2), because of the inextricable relationship to police and governmental power. 123 F.3d 591, 598-99. But see, Hillis Motors v. Hawaii Automobile Dealers, 997 F.2d 581, 591 (Ninth Cir. 1993) (There is no governmental, police power exception to 362 (a) (3)).

C. 11 U.S.C. § 362 (a) (3) automatic stays no longer constrain the exercise of police or regulatory power because the Bankruptcy Code was amended.

Bankruptcy debtors seeking to frustrate the exercise of police and regulatory power relied

upon subsection (a) (3)'s possession and control of property automatic stay since subsections (b) (4) and (5) did not expressly include an (a) (3) exception. See, discussion regarding (a) (3) in Javens v. City of Hazel Park, 107 F.3d at 367-71 (Sixth Cir. 1997) and, Hillis Motors v. Hawaii Automobile Dealers, 997 F.2d 581, 591 (Ninth Cir. 1993) (There is no governmental, police power exception to 362 (a) (3)) and Shimer v. Fugazy, 124 B.R. 426 (S.D. N.Y. 1991) Parties can no longer rely upon (a) (3) to stay the exercise of governmental and police power regarding their assets. As a result, the Consumer Advocate Division withdraws any language or suggestions in its earlier motion regarding restraint in determining consumer damages.

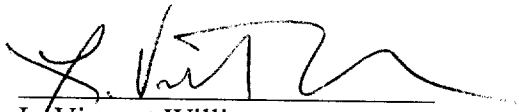
On October 21, 1998, subsection (b) (4) of the bankruptcy code was amended to combine former subsections (b) (4) and (b) (5), to expressly exempt from the automatic stay the exercise of police or regulatory power by governmental units which results in possession or control of property, and to insert language exempting all actions or proceedings regarding Chemical Weapons from the automatic stay. The subsection now reads:

> (4) under paragraph (1), (2), (3), or (6) of subsection (a) of this section, **of the commencement or continuation of an action or proceeding by a governmental unit** or any *organization* exercising authority under the Convention on the Prohibition of the Development, Production, Stockpiling and Use of Chemical Weapons and on Their Destruction opened for signature on January 13, 1993, **to enforce such governmental unit's police or regulatory power**, including **the enforcement of a judgment other than a money judgment, obtained in an action or proceeding by a governmental unit to enforce such governmental unit's police or regulatory power**.

As a result of the amendment, the exceptions from the automatic stay were expanded from subsections (a) (1) and (a) (2) to subsections (a) (1), (2), (3), and (6) while the exemption was also expanded to include chemical weapons "organization[s]."

The Consumer Advocate Division respectfully submits: that the March 26, 1999 letter of MRP is another "red herring" allowing the company to prolong its unlawful exploitation of Tennessee consumers; that the Tennessee Regulatory Authority should exercise its regulatory and police power and find that MRP has violated statutes, rules and orders of the State of Tennessee; that MRP failed to show cause why its certificate of authority should not be revoked, and that civil penalties should not be assessed; and that damages and restitution should be awarded to Tennessee consumers.

Respectfully Submitted,



L. Vincent Williams
Deputy Attorney General-Consumer Advocate
Consumer Advocate Division
425 Fifth Ave., North, Second Fl.
Nashville, TN 37243
Fax: (615) 741-8724

CERTIFICATE OF SERVICE

I, L. Vincent Williams, hereby certify that a copy of the foregoing Petition was served on the following parties of record by depositing a copy of the same in the United States mail, postage prepaid, addressed to them, in accordance with the following list, this 14th day of April, 1999:

Walter Dierks, Esq.
Sara Colley, Esq.
Jerry Colley, Esq.
Counsel for Minimum Rate Pricing
1333 New Hampshire Avenue, N.W.
Washington, DC 20036

Gary Hotvedt, Esq.
Tennessee Regulatory Authority
460 James Robertson Parkway
Nashville, TN. 37243

Rochelle Weisburg, Esq.
Angel and Frankel, P. C.
460 Park Avenue
New York, NY 10022-1906
Fax: (212) 752-8393

Richard Collier, Esq.
General Counsel
TN Regulatory Authority
460 James Robertson parkway
Nashville, TN.. 37243-0505
Fax: (615) 741-5015

L. Vincent Williams

RUBIN, WINSTON, DIERCKS, HARRIS & COOKE, L.L.P.
A REGISTERED LIMITED LIABILITY PARTNERSHIP INCLUDING PROFESSIONAL CORPORATIONS
ATTORNEYS AT LAW
TENTH FLOOR
1333 NEW HAMPSHIRE AVENUE, N.W.
WASHINGTON, D.C. 20036
(202) 861-0870
FAX: (202) 429-0657

April 2, 1999

**BY FACSIMILE, FEDERAL EXPRESS,
AND U.S. EXPRESS MAIL**

Mr. K. David Waddell
Executive Secretary
Tennessee Regulatory Authority
460 James Robertson Parkway
Nashville, TN 37243-0505

Re: **Docket No. 98-00018**
Show Cause Proceeding Against Minimum Rate Pricing, Inc.

Dear Mr. Waddell:

This is to inform the Tennessee Regulatory Authority that Minimum Rate Pricing, Inc., the subject of the above-captioned Show Cause Proceeding, filed a petition under Chapter 11 of the Bankruptcy Code, 11 U.S.C. Section 1101, *et seq.*, on February 26, 1999. A copy of the first page of the MRP petition is enclosed for your information.

Please be advised that the instant Show Cause proceeding has been automatically stayed by Section 362 of the Bankruptcy Code, 11 U.S.C. Section 362. I call to the Authority's attention *Fugazy Express, Inc. v. Shimer*, 124 B.R. 426 (S.D.N.Y. 1991), *appeal dismissed*, 982 F.2d 769 (2d Cir. 1992). Any issue regarding the scope and effect of the automatic stay and any request for relief from the automatic stay must be presented to and resolved by the United States Bankruptcy Court for the District of New Jersey, Newark Division.

Because this proceeding has been stayed, MRP is not filing a response to the Motion for Exercise of Police and Regulatory Authority to Protect the Public Interest, which was filed in violation of the automatic stay on March 24, 1999 by the Consumer Advocate Division of the Office of the Attorney General and Reporter. We believe that the substance of the CAD's Motion is subject to the stay.

RUBIN, WINSTON, DIERCKS, HARRIS & COOKE, L.L.P.

Please direct all correspondence regarding the MRP bankruptcy or the automatic stay to MRP's bankruptcy counsel:

Bruce Frankel, Esq.
Angel & Frankel, P.C.
460 Park Avenue
New York, N.Y. 10022-1906
Telephone: (212) 752-8000

I further request that a copy of this letter be placed in the docket for the above-captioned proceeding.

Very truly yours,

Walter E. Diercks

cc: L. Vincent Williams, Esq. (with enclosures)
Carla G. Fox, Esq. (with enclosures)
Bruce Frankel, Esq. (without enclosures)

---- United States Bankruptcy Court ---------- VOLUNTARY PETITION ---
DISTRICT OF NEW JERSEY
NEWARK DIVISION

IN RE ----------	NAME OF JOINT DEBTOR ----------
Minimum Rate Pricing, Inc.	N/A
ALL OTHER NAMES ----------	ALL OTHER NAMES ----------
None	N/A
SOC. SEC./TAX I.D. NO. ----------	SOC. SEC./TAX I.D. NO. ----------
22-~~3488800~~ 3358629	N/A
STREET ADDRESS OF DEBTOR ---------	STREET ADDRESS OF JOINT DEBTOR ----
150 Commerce Road	N/A
Cedar Grove, NJ 07009	
COUNTY -------- TEL-(973) 857-4200	COUNTY -------- TEL- N/A
Essex	N/A
MAILING ADDRESS OF DEBTOR --------	MAILING ADDRESS OF JOINT DEBTOR ---
150 Commerce Road	N/A
Cedar Grove, NJ 07009	

LOCATION OF PRINCIPAL ASSETS OF BUSINESS DEBTOR ----------
N/A

VENUE ----------
Debtor has been domiciled or has had a residence, principal place of business, or principal assets in this District for 180 days immediately preceding the date of this petition or for a longer part of such 180 days than in any other District.

---------- INFORMATION REGARDING DEBTOR ----------	CHAPTER OF BANKRUPTCY CODE UNDER WHICH THE PETITION IS FILED: 11
TYPE: Corporation: NOT publicly held	FILING FEE
NATURE: Business	Attached
A. TYPE OF BUSINESS	
Other Business	
B. BRIEFLY DESCRIBE NATURE OF BUSINESS	
Reseller of telecommunications services	
STATISTICAL/ADMINISTRATIVE INFORMATION---	ATTORNEY NAME(S)/ADDRESS --
Debtor estimates that, after any exempt property excluded and administrative expenses paid, NO funds will be available for distribution to unsecured creditors.	Louis Pashman
	Bar #LP-1009
---------- range -- (card code)-	PASHMAN STEIN
NO. OF CREDITORS 100-199 (4)	45 Essex Street
ASSETS (thousands) 10,000-99,999 (6)	Hackensack, NJ 07601
LIABIL. (thousands) 100,000-over (7)	
NO. OF EMPLOYEES 0 (1)	(201) 488-8200
EQUITY SEC. HOLDERS 1-19 (2)	

THIS SPACE FOR COURT USE ONLY

FILED
99 FEB 26 AM 10:49
U.S. BANKRUPTCY COURT
NEWARK, N.J.
JAMES J. WALDRON
CLERK
BY DEPUTY CLERK

CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing letter was served on the following parties of record on April 2, 1999 by facsimile, Federal Express and U.S. Express Mail by sending the facsimile copy to the facsimile machine of the recipient, placing the overnight courier copy in the possession of Federal Express and depositing the mail copy in the United States mail, postage pre-paid:

Carla G. Fox, Esq.
Tennessee Regulatory Authority
460 James Robertson Parkway
Nashville, TN 37243-0505

L. Vincent Williams, Esq.
Deputy Attorney General-Consumer Advocate
Consumer Advocate Division
Second Floor
425 Fifth Avenue, North
Nashville, TN 37243

Sarah B. Colley

RUBIN, WINSTON, DIERCKS, HARRIS & COOKE, L.L.P.
A REGISTERED LIMITED LIABILITY PARTNERSHIP INCLUDING PROFESSIONAL CORPORATIONS
ATTORNEYS AT LAW
TENTH FLOOR
1333 NEW HAMPSHIRE AVENUE, N.W.
WASHINGTON, D.C. 20036
(202) 861-0870
FAX: (202) 429-0657

March 26, 1999

VIA HAND DELIVER

Ms. Dorothy Attwood, Chief
Common Carrier Bureau
Federal Communication Commission
445 12th Street SW - The Portals
Washington, D.C.

Dear Ms. Attwood:

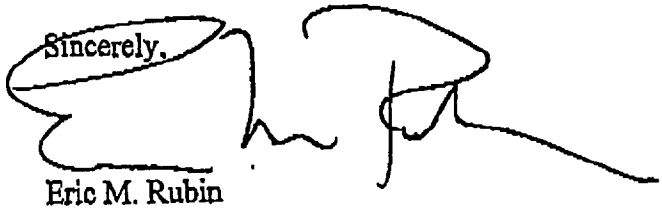
Minimum Rate Pricing, Inc. hereby submits this Compliance Report pursuant to paragraph 9(r) of NAL/Acct. No. 816EF001 for the period January 16, 1999-March 16, 1999. During the reporting period, MRP has not engaged in outbound telemarketing of Long Distance Telephone service during the reporting period. Accordingly, MRP does not have any material matters to report regarding the obligations of the Order as they pertain to such marketing activities.

During the reporting period, MRP provided marketing services to Flat Rate Long Distance, Inc., a third party engaged in marketing long distance telephone service pursuant to a business format relying on general consumer advertising designed to elicit inbound telephone response to an 800 number. MRP provided operator response, account administration and marketing services to that Company. On February 22, 1999, MRP's parent company Discount Call Waiting Inc., acquired Flat Rate Long Distance and continued these operations based on the same inbound response telemarketing format. Enclosed for your information is a copy of the general circulation advertising being disseminated for this product and a copy of the telemarketing response to inbound consumer inquiries.

RUBIN, WINSTON, DIERCKS, HARRIS & COOKE, L.L.P.

MRP has filed for reorganization under Chapter 11 of the Bankruptcy Act. As a result, all matters pertaining to the Company's operations are subject to the jurisdiction of the United States Bankruptcy Court for the Northern District of New Jersey. As you are aware, MRP was successful in securing the Courts approval of the company's plan to continue the voluntary payment provided in paragraph 3 of the Order.

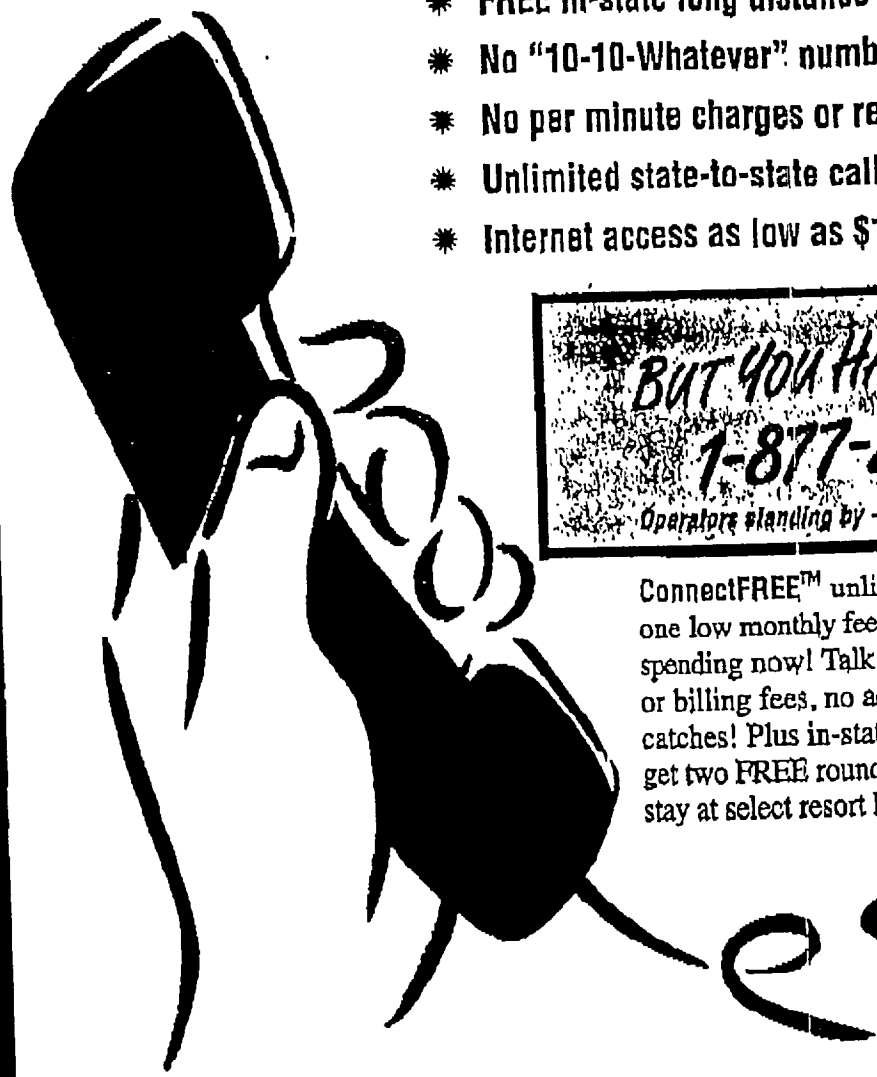
Sincerely,



Eric M. Rubin

SmartSource Magazin

This Ad Will Severely Reduce Your Phone Bill!



- FREE in-state long distance calling!
- No "10-10-Whatever" numbers to dial!
- No per minute charges or restrictions!
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- Internet access as low as $10.95/month!

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www.connectfree.com

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Domestic US calls only. Prior bill registration required. Personal residential use only. No business, data, or work related long distance use. Call fo unbelievable business plans. Taxes and government mandated carrier fees not included. Airline tickets available to customers in good standing o their third month's anniversary. Other terms and conditions apply, call for details or see our terms and conditions brochure. ©1998 Connect Free,

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FREE

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free

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- ✷ No Billing Service Fees!
- ✷ GUARANTEED to be LESS Than You're Spending Now!

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CALLER CODE [redacted]

Domestic US calls only. Prior bill registration required. Personal residential use only. No business, data, or work related long distance use. Call for unbelievable business plans. Taxes and government-mandated carrier fees not included. Services prepaid and not available in all states. Other terms and conditions apply; call for details or see our terms and conditions brochure. © 1998 Connect Free, Inc.

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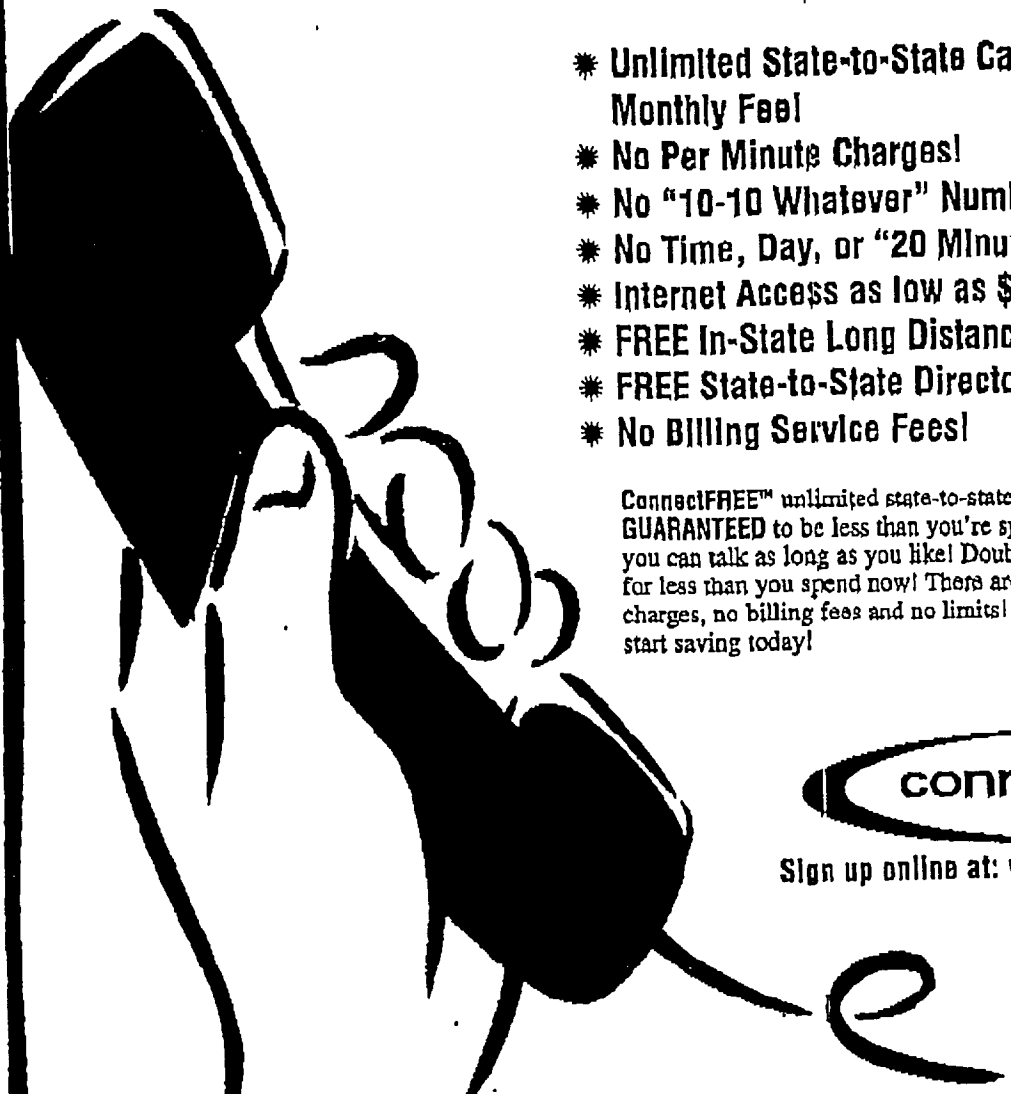

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- No Per Minute Charges!
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ConnectFREE™ unlimited state-to-state residential long distance is GUARANTEED to be less than you're spending now! But what's more is you can talk as long as you like! Double, triple, or quadruple your calls for less than you spend now! There are no sign up fees, no activation charges, no billing fees and no limits! Call 1-877-274-FREE now and start saving today!

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Domestic US calls only. Prior bill registration required. Personal residential use only. No business, data, or work related long distance use. Ca for unbelievable business plans. Texas and government-mandated carrier fees not included. All services prepaid. Other terms and conditions apply, call for details or see our terms and conditions brochure. © 1998 Connect Free, Inc.

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INBOUND SALES

FINAL REVISION
Revised 3/15/99 1:30 pm las 1

ConnectFREE Script

Greeting:

Hello, thank you for calling ConnectFree, the only unlimited long distance company. My name is _____,

Can I have the caller code # in the bottom left hand corner of your ad, _____. And who do I have the pleasure of speaking with?

_____.

And your main telephone number is?

(Note: Cannot move forward without it.)

What was it about the ad that caught your attention? Great!

Would you like to hear how the program works?

Action: If customer says yes and its about "6.9 cent" go to 6.9 specific usage offer.

Great! With ConnectFREE, you can make unlimited domestic long distance calls for one low price including free in-state long distance, no billing fees, no per minute charges, and free directory assistance. Shall I continue?

May I have your zip code? [ ]

QUALIFIER:

And, how much do you currently spend on long distance per month $ [ ] [ ] International Usage (If Given)
And that's your total long distance for all your lines, correct? [GET ANSWER YES/NO]

To Determine Usage

Customer says: I don't know my usage.
Respond: That's fine sir/ma'am, until you look it up in your records, would you estimate your current usage as $25 to $50, $50 to $100 or $150 or more.
Note: You must continue discussing their previous months usage until customer gives you a figure.
Action: If usage is lower than $12.95 minimum plan, computer will go to Rebuttal Bridge # 1.
Customer says: I still have no idea how much I spend per month.
Action: After 3 unsuccessful attempts to get usage, go to Exit Upsell
Customer says: I spend over $150.00
Action: Computer goes to Rebuttal Bridge # 2

If not interested, go to Exit Upsell

ZIP CODE:

Is that zip code for [(city)], [(state)]? Ok, sir/ma'am, in order for me to see if we can provide service in your area may I have your street address there, including apartment number? [ ]
Thanks!

(Note: Cannot move forward without address) Note: Program must mark address as "R" or "B".

Super! Now _____, are you calling about your business, home office or residence?

Customer Says: I am calling for Business/home office.
Action: Computer goes to Rebuttal Bridging #3

Unlimited Personal Plan:

Now, while the computer is calculating your unlimited rate, let me explain. For one low price, you can now make as many residential domestic call as you want, whenever you want and talk as long as you want including free in-state long distance calls. There are no billing service fees, no per minute charges, and directory assistance is also free. [Now, Mr./Mrs. _____ as you said, you spend $ _____ per month, correct? For example with ConnectFREE, make three (3) or four (4) times as many calls for only $ _____, conveniently billed to your credit card or checking account.] Of course, normal taxes and government mandated carrier fees apply, but there are no billing fees, no extra charges and no surprises! Do you understand the benefits of the unlimited plan. (If not, repeat formula again.)

If yes, Computer goes to Data Entry Read Back.
If no, go to ConnectFREE 6.9 cent Calling Plan C.

Ok, Mr/Ms _____ due to your special situation, I can offer you the lowest unrestricted rate in the county – 6.9 cents all the time. Let me tell you ho it works.

ConnectFREE 6.9 Cent Calling Plan (A)

Now, here is how it works, all your calls are at just 6.9 cents per minute out of state and only 10 cents per minute for in state long distance. As an additional benefit, we establish your account at less than your spending now. You said you spend $_____, correct? Ok, we take 25% off that establishing your account at $ _____ worth of calling. Your minutes will be deducted from this amount as you use them. (For Business Customers Only: To administer this super low rate, there is a one-time set up fee of just $19.95). To maximize your savings, any leftover minutes carry forward and are always refundable – so you never lose anything. To insure your uninterrupted service, your account is automatically recharged before it runs out and best of all, this is the lowest unrestricted rate in the country with a $4.95 fee! Only normal taxes and government mandated carrier fees apply. Do you understand how the 6.9 cent plan works? (If not sure repeat formula again slowly.)

6.9 Cents Per Minute (total min.) or 10 Cents Per Minute (total min) (information for rep use, if needed)

If yes, go to Data Entry Read Back
If no, go to Exit Upsell

INBOUND SALES

FINAL REVISION
Revised 3/15/99 1:30 pm las 2

ConnectFREE Script

DATA ENTRY & READ

So, let me confirm some information and you can try our service under our risk free money back guarantee, ok?

1. And your main phone number (AREA CODE AND PHONE NUMBER) is your home number, right?
2. And the address is (STREET, CITY, STATE, ZIP).
3. And the spelling of the billing name is (SPELL OUT FULL NAME), is that you sir/ma'am?
   If not, ask for the full spelling of the caller's name.
4. And Sir/Ma'am if any unauthorized person should try to make changes to your phone acct., do you have an alternate phone number where we can reach you or your spouse? (GET NUMBER,AREA CODE AND PHONE NUMBER)
5. And your e-mail address is: (E-MAIL ADDRESS)

Now Sir/Ma'am with your service billed to VISA, MasterCard, American Express, Discover, automatic checking you can receive a bonus of one (1) free month of service! Which payment method would you prefer?

Choose One:
CC ☐
AC ☐
DB ☐

If neither payment method is produced:
Go to Electronic Payment Rebuttal Dialogue.
Note: If choice is DB this verbiage box will appear:
Now Mr./Ms. _____ we are happy to accommodate you, and I welcome you as a potential long term customer. However, please understand that the direct billing computer process is not flexible and to avoid any interruptions in your Connect Free service our invoice is payable upon receipt. As always, if you're dissatisfied for any reason you have our 100% 30 day money back guarantee. OK?

BOX 1 If Credit Card Complete:

Enter Card Type
MasterCard ☐
Visa ☐
American Express ☐
Discover ☐
Diners Club ☐

And your account number is: ☐☐☐☐☐☐☐☐☐☐☐☐☐☐☐☐

And your expiration date is: ☐☐ ☐☐

And the cardholders name as it appears on the card is:

Note: If credit card name is different from the caller, say:
And your relationship to the cardholder is:

If card holder is not the spouse, offer automatic checking option. If no checking account – offer direct billing!

Combination: CC/Debit

BOX 2 If Automatic Checking Complete:

And the name of your Bank is

Now, sir/ma'am, I need your account number. Do you have a check handy?

Ok, sir/ma'am, what's the check # on that check?
☐☐☐☐

Now, look at the bottom of that check, can you please give me your account #?
☐☐☐☐☐☐☐☐☐☐
☐☐☐☐☐☐☐☐☐☐

Ok, please read off the other large group of numbers minus the check # - they should be the numbers in between the columns.
☐☐☐☐☐☐☐☐☐

Now, for your own record keeping, please void out that check

And the name on the account as it appears on the check:

Note: If checking account name is different from the caller, say: And your relationship to the person's name on the account is:

If name on the checking account is not the spouse, offer credit card option. If no credit card – offer direct billing!

BOX 3 If Direct Billing Complete

Now is your direct billing address the same as we discussed?:

yes no

If no, get proper billing address:

Preparation for Order Confirmation :
O.K. Mr./Ms. _____, now all I need to do to activate your ConnectFree Service and mail you a written confirmation is to confirm the information we just went over. I will be taping it for accuracy, so please let me know if the information I have is correct, it'll only take a minute. Before we begin do you have any questions?

Note: If caller states at any point they are not interested in long distance, go to exit upsell script.

INBOUND SALES

FINAL REVISION
revised 3/15/99 1:30 pm las 3

Rebuttal Bridging 1
Usage Lower Than 12.95

ZIP CODE:

Is that Zip Code for [(city)], [(state)]? Great, and what is your street address there, including apartment number? [ ] Thanks!

(Note: Cannot move forward without address)

Now, Mr./Ms. _____, are you calling about your business, home office, or residence?

Customer Says: I am calling for Business/home office.
Action: Computer goes to Rebuttal Bridging #6

Minimum Unlimited Personal Plan

OK, sir/ma'am the lowest plan we have available is $12.95/month and you can make all the calls you want, whenever you want, and talk as long as you want, including free in-state long distance. There are no billing service fees, no per minute charges, and directory assistance is also free. Now, Mr./Ms. _____ as you said, you spend $ _____ per month. Correct? With ConnectFREE, make three (3) or four (4) times as many calls for only $ 12.95, conveniently billed to your credit card or checking account. Of course, normal taxes and government mandated carrier fees apply, but there are no billing fees, no extra charges and no surprises!

If yes, go to Data Entry Read Back.
If no, go to 6.9 Cent Plan (B)

ConnectFREE 6.9 Cent Calling Plan (B)

OK, sir/ma'am because of your special situation, I can offer you the lowest unrestricted per minute rate in the country. Now, here is how it works, c your calls are at just 6.9 cents per minute out of state- that's over 75% off AT&T's Basic Rates, and in-state long distance calls are just 10 cents per minute. We establish your account at $16.00 worth of calling. Your minutes will be deducted from this amount as you use them. To maximize you savings, any leftover minutes carry forward and are always refundable –so you never lose anything. To insure your uninterrupted service, your account is automatically recharged before it runs out and best of all, this is the lowest unrestricted rate in the country with a $4.95 fee Only normal taxes and government mandated carrier fees apply. Do you understand how the 6.9 cent plan works? (If not sure repeat formula again slowly.)

If no, go to Exit Upsell
If yes, go to Data Entry Read Back

INBOUND SALES

FINAL REVISIO
revised 3/15/99 1:30 pm las

ZIP CODE

Rebuttal Bridging 2
Over $150 of Usage

Is that Zip Code for (city), (state)? Great, and what is your street address there, including apartment number? Thanks!

(Note: Cannot move forward without address)

Now, Mr./Ms. _____, are you calling about your business, home office, or residence.

Customer Says: I am calling for Business/home office.
Action: Computer goes to Rebuttal Bridging #6

This customer spends over $150.00, responds:

Ok Mr./Ms _____ one of the initial requirements for the unlimited plan is a maximum usage of $150. Since you exceed this amount the best way I can service you today is through our special usage plan. There are no contracts, no long-term commitments, or discounts that never deliver the savings that you were promised. With us it's simple and inexpensive at 6.9 cents per minute. That's over 75% off AT&T's Basic Rates and it is the lowest unrestricted rate in the country! All conveniently billed to the credit card or checking account of your choice, let me tell you how it works.

ConnectFREE 6.9 Cents Calling Plan (A)

Now, here is how it works, all your calls are at just 6.9 cents per minute out of state and only 10 cents per minute for in state long distance. As an additional benefit, we establish your account at less than your spending now. You said you spend $_____, correct? Ok, we take 25% off that, establishing your account at $ _____ worth of calling. Your minutes will be deducted from this amount as you use them. (For Business Customers Only: To administer this super low rate, there is a one-time set up fee of just $19.95). To maximize your savings, any leftover minutes carry forward and are always refundable – so you never lose anything. To insure your uninterrupted service, your account is automatically recharged before it runs out; and best of all, this is the lowest unrestricted rate in the country with a $4.95 fee! Only normal taxes and government mandated carrier fees apply. Do you understand how the 6.9 cent plan works? (If not sure repeat formula again slowly.)

6.9 Cents Per Minute (total min.) ☐ or 10 Cents Per Minute (total min) ☐ (Information for rep use, if needed)

If yes, go to Data Entry Read Back
If no, go to Exit Upsell

INBOUND SALES

FINAL REVISION
revised 3/15/99 1:30 pm las S

Rebuttal Bridging 3:
Business, HomeOffice User

Note: If customer is a home office or business user, respond:
The unlimited long distance offer with FREE in-state long distance calling is a residential plan only. But, due to your special situation I can offer you the lowest unrestricted rate in the country, 6.9 cents all the time. Shall I continue?

HOW:

There are no contracts, no long-term commitments, or discounts that never deliver the savings that you were promised. With us it's simple and inexpensive at 6.9 cents per minute. That's over 75% off AT&T's Basic Rates! All conveniently billed to the credit card or checking account of your choice.

ConnectFREE 6.9 Cent Calling Plan (C)

Now, here is how it works, all your calls are at just 6.9 cents per minute out of state and only 10 cents per minute for in state long distance. As an additional benefit, we establish your account at less than your spending now. You said you spend $_____, correct? Ok, we take 25% off that establishing your account at $ _____ worth of calling. Your minutes will be deducted from this amount as you use them. To administer this super low rate, there is a one-time set up fee of just $19.95. To maximize your savings, any leftover minutes carry forward and are always refundable – so you never lose anything. To insure your uninterrupted service, your account is automatically recharged before it runs out and best of all, this is the lowest unrestricted rate in the country with a $4.95 fee! Only normal taxes and government mandated carrier fees apply. Do you understand how the 6.9 cent plan works? (If not sure repeat formula again slowly.)

6.9 Cents Per Minute (total min,) ☐ or 10 Cents Per Minute (total min) ☐ (information for rep use, if needed)

If yes, go to Data Entry Read Back
If no, go to Exit Upsell

INBOUND SALES **Inbound Pager Stand Alone Script** **FINAL VERSION**
Revised 3/15/99 1:30 pm jas

Introduction

Now as a preferred customer, you're entitled to a FREE Motorola/NEC pager with one month of FREE unlimited paging! The pager is FREE with a one time activation and shipping fee of only $29.95! After your free month, the pager's yours to keep! You may continue unlimited paging for $9.95 per month or cancel at any time, and the pager is our gift. Would you like one?

Pager Quantity ☐

Note: (If yes, respond: O.K. is one enough)?

NOTE: Pagers will be shipped to the problem molester address entry!

DATA ENTRY & READ BACK

So, let me confirm some information and you can try our service under our risk free money back guarantee, ok?
1. And your main phone number (AREA CODE AND PHONE NUMBER) is your home number, right?
2. And the address is (STREET, CITY, STATE, ZIP).
3. And the spelling of the billing name is (SPELL OUT FULL NAME), is that you sir/ma'am?
   If not, ask for the full spelling of the caller's name.
4. And the daytime number that you can be reached at is: (AREA CODE AND PHONE NUMBER)
5. And your e-mail address is: (E-MAIL ADDRESS)

Now Sir/Ma'am with your service billed to VISA, MasterCard, American Express, Discover, automatic checking you can receive a bonus of one (1) free month of service! Which payment method would you prefer?

Choose One:
CC ☐
AC ☐
DB ☐

If neither payment method is produced:
Go to Electronic Payment Rebuttal Dialogue.
Note: If choice is DB this verbiage box will appear:
Now Mr./Ms. _____ we are happy to accommodate you, and I welcome you as a potential long term customer. However, please understand that the direct billing computer process is not flexible and to avoid any interruptions in your Connect Free service our invoice is payable upon receipt. As always, if you're dissatisfied for any reason you have our 100% 30 day money back guarantee. OK?

BOX 1 **If Credit Card Complete**

Enter Card Type
MasterCard ☐
Visa ☐
American Express ☐
Discover ☐
Diners Club ☐

And your account number is: _____

And your expiration date is: ☐☐ ☐☐

And the cardholders name as it appears on the card is: _____

Note: If credit card name is different from the caller, say:
And your relationship to the cardholder is: _____

If card holder is not the spouse, offer automatic checking option. If no checking account – offer direct billing!

Combination: CC/Debit Card

BOX 2 **If Automatic Checking Complete:**

And the name of your Bank is

Now, sir/ma'am, I need your account number. Do you have a check handy?

Ok, sir/ma'am, what's the check # on that check? ☐☐☐☐

Now, look at the bottom of that check, can you please give me your account #? ☐☐☐☐☐☐☐☐☐☐

Ok, please read off the other large group of numbers minus the check # - they should be the numbers in between the columns. ☐☐☐☐☐☐☐☐☐

Now, for your own record keeping, please void out that check.

And the name on the account as it appears on the check: _____

Note: If checking account name is different from the caller, say: And your relationship to the person's name on the account is: _____

If name on the checking account is not the spouse, offer credit card option. If no credit card – offer direct billing!

BOX 3 **If Direct Billing Complete**

Now is your direct billing address the same as we discussed?

yes no

If no, get proper billing address:

INBOUND SALES **Inbound Pager Stand Alone Script** **FINAL VERSIO**
Revised 3/15/99 1:30 pm lpa

Preparation for Verification:

O.K. Mr./Ms. _____, now all I need to do to activate your FREE pager is to verify the information we just went over. I will be taping it for accuracy, it'll only take a minute. Before we begin do you have any questions?

COURTESY CLOSE: OK Mr./Mrs. _____, thank you for calling in today. If you have any other questions regarding our services in the future, please call us back at : (1-877-274-3733) or visit our web site WWW.ConnectFree.com. Have a nice day.

INBOUND SALES

FINAL REVISION
revised 3/15/99 1:30 pm las 8

DATA ENTRY & READ BACK

So, let me confirm some information and you can try our service under our risk free money back guarantee, ok?
1. And your main phone number (AREA CODE AND PHONE NUMBER) is your home number, right?
2. And the address is (STREET, CITY, STATE, ZIP).
3. And the spelling of the billing name is (SPELL OUT FULL NAME), is that you sir/ma'am?
   If not, ask for the full spelling of the caller's name.
4. And the daytime number that you can be reached at is: (AREA CODE AND PHONE NUMBER)
5. And your e-mail address is: (E-MAIL ADDRESS)

Now Sir/Ma'am with your service billed to VISA, MasterCard, American Express, Discover, automatic checking you can receive a bonus of one (1) free month of service! Which payment method would you prefer?

Choose One:
CC ☐
AC ☐
DB ☐

If neither payment method is produced:
Go to Electronic Payment Rebuttal Dialogue.
Note: If choice is DB this verbiage box will appear:
Now Mr./Ms. _____ we are happy to accommodate you, and I welcome you as a potential long term customer. However, please understand that the direct billing computer process is not flexible and to avoid any interruptions in your Connect Free service our invoice is payable upon receipt. As always, if you're dissatisfied for any reason you have our 100% 30 day money back guarantee. OK?

BOX 1 If Credit Card Complete:

Enter Card Type
MasterCard ☐
Visa ☐
American Express ☐
Discover ☐
Diners Club ☐

And your account number is: _____

And your expiration date is: ☐☐ ☐☐

And the cardholders name as it appears on the card is: _____

Note: If credit card name is different from the caller, say:
And your relationship to the cardholder is: _____

If card holder is not the spouse, offer automatic checking option. If no checking account – offer direct billing!

Combination: CC/Debit

BOX 2 If Automatic Checking Complete:

And the name of your Bank is

Now, sir/ma'am, I need your account number. Do you have a check handy?

Ok, sir/ma'am, what's the check # on that check? ☐☐☐☐

Now, look at the bottom of that check, can you please give me your account #?

☐☐☐☐☐☐☐☐☐☐
☐☐☐☐☐☐☐☐☐☐

Ok, please read off the other large group of numbers minus the check # - they should be the numbers in between the columns.

☐☐☐☐☐☐☐☐☐

Now, for your own record keeping, please void out that check

And the name on the account as it appears on the check: _____

Note: If checking account name is different from the caller, say: And your relationship to the person's name on the account is: _____

If name on the checking account is not the spouse, offer credit card option. If no credit card – offer direct billing!

BOX 3 If Direct Billing Complete

Now is your direct billing address the same as we discussed?

yes no

If no, get proper billing address:

_____

_____

Preparation for Verification:
O.K. Mr./Ms. _____, now all I need to do to activate your ConnectFree Special Pricing Plan of 6.9 cents per minute and mail you your written confirmation will be to verify the information we just went over. I will be taping it for accuracy, so please let me kno If it is correct, it'll only take a minute. Before we begin do you have any questions?

Note: If caller states at any point they are not interested in long distance, go to exit upsell script!

INBOUND SALES **Exit Up-sell Script** FINAL VERSION 9
Revised 3/15/99 1:30. las

Privacy Minder Offer

O.K. Mr./Ms. _____ before I go, I'm required to inform you about your right to Privacy Minder service. It's a consumer benefit that guarantees your right to privacy by stopping the thousands of aggressive telemarketing companies who forcefully try selling you things you don't want and don't need! Privacy Minder puts an end to all the interruptions that inconvenience you and waste your personal time. By utilizing federal laws, we contact over 3,000 telemarketing companies and remove your name from their computers!

This service is absolutely FREE for the first 3 months to give you plenty of time to evaluate your new found peace. Then PrivacyMinder continues to protect you from telemarketers at the annual rate of $39.95 – less than $3.50 a month, unless canceled.

Now sir/ma'm, you no longer want to receive these types of annoying calls at home, do you?
O.K. Great! Should we start your FREE trial of PrivacyMinder today?
Note: If customer wants to end the call: Go to Courtesy Close.

Decision	
Yes	No
☐	☐

If the caller has an e-mail or computer the following question screen will pop up.
Question:
Sir/Ma'am would you like to hear how you can receive internet access at one of the lowest rates in the country? Yes ☐ No ☐
If yes go to internet script, if no continue

Pager

Now, as a preferred customer, you're entitled to a FREE motorola/NEC pager with one month of FREE unlimited paging! The pager is FREE with a one time activation and shipping fee of only $29.95! After your free month, the pager's yours to keep! You may continue unlimited paging for only $9.95 per month or cancel at any time, and the pager is our gift. Would you like one?

Pager quantity
Note: (If yes, repond: OK, is one enough?)

DATA ENTRY & READ BACK

So, let me confirm some information and you can try our service under our risk free money back guarantee, ok?
1. And your main phone number is (AREA CODE AND PHONE NUMBER?) And this is your home or business number, right?
2. And the address is (STREET, CITY, STATE, ZIP).
3. And the spelling of the billing name is (SPELL OUT FULL NAME), is that you sir/ma'am?
   If not, ask for the full spelling of the caller's name.
4. And the daytime number that you can be reached at is: (AREA CODE AND PHONE NUMBER)
5. And your e-mail address is: (E-MAIL ADDRESS)

Now Sir/Ma'am with your service billed to VISA, MasterCard, American Express, Discover, automatic checking you can receive a bonus of one (1) free month of service! Which payment method would you prefer?

Choose One:	
CC	☐
AC	☐
DB	☐

If neither payment method is produced:
Go to Electronic Payment Rebuttal Dialogue.
Note: If choice is DB this verbiage box will appear:
Now Mr./Ms. _____ we are happy to accommodate you, and I welcome you as a potential long term customer. However, please understand that the direct billing computer process is not flexible and to avoid any interruptions in your Connect Free service our invoice is payable upon receipt. As always, if you're dissatisfied for any reason you have our 100% 30 day money back guarantee. OK?

BOX 1 If Credit Card Complete:

Enter Card Type

MasterCard ☐
Visa ☐
American Express ☐
Discover ☐
Diners Club ☐

And your account number is: _____

And your expiration date is: ☐☐ ☐☐

And the cardholders name as it appears on the card is: _____

Note: If credit card name is different from the caller, say:
And your relationship to the cardholder is:: _____

If credit card is for other than the spouse, offer checking account option. If no checking account – offer direct billing!

Combination: CC/Debit Card

BOX 2 If Automatic Checking Complete:

And the name of your Bank is _____

Now, sir/ma'am, I need your account number. Do you have a check handy?
Ok, sir/ma'am, what's the check # on that check? ☐☐☐☐

Now, look at the bottom of that check, can you please give me your account #? ☐☐☐☐☐☐☐☐☐☐

Ok, please read off the other large group of numbers minus th check # - they should be the numbers in between the colons. ☐☐☐☐☐☐☐☐☐

Now, for your own record keeping, please void out that check.

And the name that appears on the check is: _____

Note: If checking account name is different from the caller, say:
And your relationship to the person's name on the account is: _____

If name on the checking account is not the spouse, offer credit card option. If no credit card – offer direct billing!

INBOUND SALES **Exit Up-sell Script** FINAL VERSION 10
Revised 3/15/99 1:30. las

BOX 3 If Direct Billing Complete
Now is your direct billing address the same as we discussed? yes no
If no, get proper billing address:

Preparation for Verification:

O.K. Mr./Ms. _____, now all I need to do to activate your ConnectFree services and mail you our written confirmation will be to verify the information we just went over. I will be taping it for accuracy, so please let me if is correct, it'll only take a minute. Before we begin do you have any questions?

COURTESY CLOSE: OK Mr./Mrs. _____, thank you for calling in today. If you have any other questions regarding our services in the future, please call us back at: (1-877-274-3733) or visit our web site at WWW.ConnectFree.com. Have a nice day.

ORDER CONFIRMATION **CONNECTFREE – LONG DISTANCE** **FINAL VERSION**]
Revised 2/12/99 12:30 pm las

***NOTE*: PRESS PLAY AND BEGIN RECORDING! Just read and let the customer confirm that the information is correct.**

Long Distance Introduction

O.K. now, I will be recording this call to insure accurate order entry of your ConnectFree order. As we discussed you will receive a written confirmation stating all your terms in writing. Should you have any questions after you review this information, just call our Customer Care Center for assistance. Now today is (Name of day, e.g. Monday) (Date: Month, day, year) and you have called to receive the Connect Free:

☐ Unlimited Personal Plan ☐ Special Usage Plan ☐☐ ☐☐ ☐☐ Date

Now, Mr./Mrs. _____ your caller code from the id is #_____, correct? Great!

1. Now, do you have the authority to approve the carrier change to Connect Free?
2. And are you authorizing the change of your long distance carrier to Connect Free long distance from your current carrier? [MUST GET RESPONSE]

ISP Introduction

O.K. now, I will be recording this call to insure accurate order entry of your ConnectFree order. As we discussed you will receive a written confirmation stating all your terms in writing. Should you have any questions after you review this information, just call our Customer Care Center for assistance. Now today is, (Name of day, e.g. Monday) and you have called to receive ConnectFree Services ☐☐ ☐☐ ☐☐ Date

Now, Mr./Mrs. _____ your caller code from the id is # _____, correct? Great!

Ok, Mr./Mrs. _____, I just wanted to confirm that you'll be receiving internet access for:

☐ $10.95 per month prepaid for 21 months ($229.95) with a one-time activation fee of $18.95.
or

☐ $13.95 per month with a one-time activation fee of $18.95

Included is our 100% money back guarantee. And, if you're dissatisfied at any time within your first 30 days of service we'll refund 100% of your internet access fee, no questions asked.

Now, you'll be receiving written confirmation with your start-up kit within the next 7 days. Included, will be everything you need to make your first connection quick and easy. OK? [GET ANSWER]

IF ALSO LONG DISTANCE ASK:

1. Now, do you have the authority to approve the carrier change to Connect Free? [GET ANSWER]
2. And are you authorizing the change of your long distance carrier to Connect Free long distance from your current carrier? [MUST GET REPONSE]

Billing Data & Read Back:

RESIDENTIAL

1a. OK, now, your name is.

And the home phone bill comes in your name, correct?

Note: If your customer is anyone other than the owner of the phone bill (or their spouse) you must ask: Now is there anyone else that needs to be involved in this decision besides yourself? (If Yes, you must get the other person's approval).

BUSINESS

1b. OK, now, your name is.

And your title is:

Note: If your customer is anyone other than the owner, spouse, president, vice president, treasurer, controller, or CEO you must ask: Now is there anyone else that needs to be involved in this decision besides yourself? (If Yes, you must get the other person's approval).

2. Your Main Telephone Number is: ☐☐☐ ☐☐☐ ☐☐☐☐ Main Number

2a. The exact billing name we have for that number is: Is that how the name appears on the local bill? Billing Name

3. And the daytime number we can reach you at is: ☐☐☐ ☐☐☐ ☐☐☐☐ Daytime Number

4. Now, the billing address I have for that location is:

Mailing Address

City ☐☐ State ☐☐☐☐☐ Zip Code

Note: For unlimited plan 2 additional lines only. For 6.9 plan 1 additional line are permitted.

5. And as you stated your current monthly long distance usage is $ ☐☐☐ correct?

ORDER CONFIRMATION **CONNECTFREE – LONG DISTANCE** **FINAL VERSION**
Revised 2/12/99 12:30 pm la

Note: Keep Recording

Emergency Calling Plan

As a customer reward you're entitled to our Emergency Calling Plan. This plan consists of a toll FREE 800 number at only 12 cents per minute for all calls made to you and includes a 12 cent, no surcharge calling card pre-loaded with 30 minutes of FREE calling. This package provides the complete emergency protection you need to stop $3.00 collect calls and allow loved ones an easy, inexpensive way to contact you. With 12 cents per minute and only a $3.95 monthly service fee, the savings are enormous!

Now, may we activate your 30 free minutes and toll free 800 number now? (Requires a yes or no response).

O.K. what phone number would you like your 800 toll free service to ring on? ☐☐☐ ☐☐☐ ☐☐☐☐

Your inbound toll free 800# sir/ma'am will permit you to receive calls from within:

a) Your State Only
b) The U.S.
c) The U.S & Canada

Which one would you prefer? (circle one)

Pick One

Emergency Calling Plan Only	Toll Free 800# Only	12 Cent Calling Card Only	12Cent Calling Card Qty. (limit 3)
☐	☐	☐	☐

(Note: $3.95 monthly service fee remains the same for all 3 choices.)

NOTE: KEEP RECORDING

Payment Method:

Now Mr./Ms. _____, you would like to pay your monthly bill with a credit card or automatic checking or direct billing, correct? (Requires a yes or no response)

NOTE: Just read and let the customer confirm that the information is correct.

BOX 1 Credit Card Confirmation

Enter Card Type

MasterCard ☐
Visa ☐
American Express ☐
Discover ☐
Diners Club ☐

And your account number is: ☐☐☐☐☐☐☐☐☐☐☐☐☐☐☐☐

And your expiration date is: ☐☐ ☐☐

And the cardholders name as it appears on the card is: ☐☐☐☐☐☐☐☐☐☐☐☐☐☐☐☐

Note: If credit card name is different from the caller, say; And your relationship to the cardholder is: ☐☐☐☐☐☐☐☐☐☐☐☐☐☐☐☐

If card holder is not the spouse, offer automatic checking option. If no checking account – offer direct billing!

Combination: CC/Debit

BOX 2 Automatic Checking Confirmation

And the name of your Bank is ☐☐☐☐☐☐☐☐☐☐☐☐☐☐☐☐

Now, sir/ma'am, I need your account number. Do you have a check handy?

Ok, sir/ma'am, what's the check # on that check? ☐☐☐☐

Now, look at the bottom of that check, can you please give me your account #? ☐☐☐☐☐☐☐☐☐☐☐☐☐☐☐☐☐☐☐☐

Ok, please read off the other large group of numbers minus the check # - they should be the numbers in between the columns. ☐☐☐☐☐☐☐☐☐☐

Now, for your own record keeping, please void out that check.

And the name on the account as it appears on the check: ☐☐☐☐☐☐☐☐☐☐☐☐☐☐☐☐

Note: If checking account name is different from the caller, say; And your relationship to the person's name on the account is: ☐☐☐☐☐☐☐☐☐☐☐☐☐☐☐☐

If name on the checking account is not the spouse, offer credit card option. If no credit card – offer direct billing!

BOX 3 If Direct Billing Complete

Now is your direct billing address the same as we discussed?
yes no
If no, get proper billing address.

ORDER CONFIRMATION **CONNECTFREE – LONG DISTANCE** **FINAL VERSION** 3
Revised 2/12/99 12:30 pm la

LD Closing:

7. Ok now, I'd like you to write down our toll free customer care number. Do you have a pen? Great it's [(877) 785-FREE]. Customer Care will be sending your written confirmation prior to your service change, so you'll have plenty of time to review the materials and make any modifications you desire. The written confirmation will guarantee your:

   Unlimited domestic calling rate of $____ in writing. Additionally, to maintain your rate you'll receive an account registration card to register a copy of your long distance phone bill from your current carrier.

   or

   Your 6.9 cent interstate plan with a monthly service fee of $4.95.

Privacy Minder:

8. Now, as a customer benefit, we're also giving you three FREE months of Privacy Minder service. Which guarantees your privacy at home by stopping the thousands of aggressive telemarketing companies that call and interrupt your personal time to sell you things you don't want. By utilizing federal laws we **do** continue over 3,000 telemarketing companies and remove your name from their computers month after month. This service is absolutely FREE for the first 3 months so you can enjoy your new found peace. Then it continues to protect you from telemarketers at a cost of only $3.33 a month, billed annually unless canceled.

   Now sir/ma'm, you no longer want to receive these types of annoying calls at home, do you?
   O.K. Great! Should we start your FREE trial of Privacy Minder today? Yes ☐ No ☐

[Note: This question will only pop up only as an upsell to LD callers as needed.]

Question: Sir/Ma'am would you like to hear how you can receive internet access at one of the lowest rates in the country? Yes ☐ No ☐
If Yes: Computer goes to ISP screen. If No: Continue.

Pager:

9. Finally, as a preferred customer benefit you're entitled to a FREE Motorola/NEC pager with one month of FREE unlimited paging! The pager is FREE as a customer reward with a one time activation and shipping fee of only $29.95! After your free month, the pager's yours to keep! You may continue unlimited paging for $9.95 per month, or cancel at any time, and keep the pager as our gift. Would you like one?

   Note: (If yes, respond: O.K. is one enough)? Pager Quantity: ☐

Summary of Charges:

For Credit Card ,Checking Account and Direct Billing, explain to the Customer the following:
OK Mr./Mrs. _____ the charges that will be applied to your credit card or automatic checking or direct billing today are:

Your recurring monthly charges consist of:	1) Unlimited LD or Special Pricing Plan:	$_____
	2) The Toll Free Emergency Calling # and Card for:	$_____
	3) Monthly internet access fee of:	$_____
	Your recurring monthly total charge is:	$_____
Your One time charge consists of:	1) The Processing Fee for the 6.9 Plan of:	$_____
	2) Your Activation and Shipping Fee for the Pager:	$_____
	3) The 10.95 per month Internet Access prepaid for 21 months which totals:	$_____
	4) An internet activation fee of:	$_____
	Your one time total charge is:	$_____

The total amount to be charged to your credit card/automatic checking will be $_____ Plus Taxes

For Unlimited Calling Plan, say:

1. Now, Mr./Mrs. _____ each month you'll get your Connect Free statement for review seven days in advance of any charge or withdrawal.

For ConnectFREE 6.9 Cent Calling Plan, say:

2. Now, Mr./Mrs. _____ your 6.9 ¢ rechargeable amount will get replenished whenever your account has only 20% left and your monthly statement will reflect all account detail.

For automatic checking must verify the following:

And just to confirm:

1. The name on the account that the charge will be withdrawn from each month is: _____. Correct?
2. And, Mr./Mrs. _____, monthly ongoing automatic payments will be deducted from your account for as long as you remain on our service? OK? **(Requires a yes or no response.)**

Closing:

Now, just for identification purposes when you call in, can I have your Social Security # ? ☐☐☐-☐☐-☐☐☐☐

If customer refuses say, may I just have the last 4 digits of your Social Security #? ☐☐☐☐

If customer still refuses say, Is the month and year of your birth ok? If no, just continue. ☐☐-☐☐

As a reminder, Mr./Ms. _____, your ConnectFREE charges will appear on your next (choose one: credit card/bank/direct billing) account statement, with our guarantee that if you are ever dissatisfied within your first 30 days of service, 100% of your domestic charges will be credited to you, no questions asked. I'd like to now thank you for calling in today and before I go Is there any other way I may service you? O.K. Thanks and Welcome to ConnectFree!

Programming note: The computer must call up either "credit card", "bank", or "direct billing" in the last paragraph

ORDER CONFIRMATION **Pager Verification (Stand Alone)** **FINAL VERSION** Revised 2/12/99 12:30 pm 4

Note: Press play and begin recording now! Just read and let the customer confirm that the information is correct.

Introduction:

Now as the last procedure for the Quality Control Department here at ConnectFree Long Distance, Inc., I will be recording this call today to insure accurate order entry. Now the reason we are speaking is to reconfirm the details you called about today, (Name of day, e.g. Monday) (Date: Month, day, year) with me (first and last name) in order to receive a FREE pager.

Date: ☐☐ ☐☐ ☐☐

O.K. Mr./Ms. _____, I just wanted to confirm that you'll be receiving a FREE Motorola/NEC Pager and one month of FREE unlimited paging.

With a one-time activation and shipping fee of only $29.95 and ongoing paging for just $9.95 per month. ***

BILLING DATA

RESIDENTIAL

1. Ok, now your name is ☐

2. Your Main Telephone Number is: ☐☐☐☐☐☐☐☐☐☐ Main Number

2a. The exact billing name we have for that number is: Is that how the name appears on the local bill? ☐ Billing Name

3. And the daytime number we can reach you at is: ☐☐☐☐☐☐☐☐☐☐ Daytime Number

***

ORDER CONFIRMATION

Pager Verification
(Stand Alone)

FINAL VERSION
Revised 2/12/99 12:30 pm 5

NOTE: KEEP RECORDING

Payment Method:

Now Mr./Ms. _____, you did state that you would like to pay your pager charges with a credit card or automatic checking or direct billing, correct?
(Requires a yes or no response)
NOTE: Just read and let the customer confirm that the information is correct.

BOX 1 — **Credit Card Confirmation**

Enter Card Type
MasterCard ☐
Visa ☐
American Express ☐
Discover ☐
Diners Club ☐

And your account number is: _____

And your expiration date is: ☐☐ ☐☐

And the cardholders name as it appears on the card is: _____

Note: If credit card name is different from the caller, say:
And your relationship to the cardholder is: _____

If card holder is not the spouse, offer automatic checking option. If no checking account – offer direct billing!

Combination: CC/Debit Card

BOX 2 — **Automatic Checking Confirmation**

And the name of your Bank is _____

Now, sir/ma'am, I need your account number. Do you have a check handy?

Ok, sir/ma'am, what's the check # on that check? ☐☐☐

Now, look at the bottom of that check, can you please give me your account #? ☐☐☐☐☐☐☐☐☐☐

Ok, please read off the other large group of numbers minus the check # - they should be the numbers in between the columns. ☐☐☐☐☐☐☐☐

Now, for your own record keeping, please void out that check.

And the name on the account as it appears on the check: _____

Note: If checking account name is different from the caller, say: And your relationship to the person's name on the account is: _____

If name on the checking account is not the spouse, offer credit card option. If no credit card – offer direct billing!

BOX 3 — **If Direct Billing Complete**

Now is your direct billing address the same as we discussed?:
yes no
If no, get proper billing address:

_____
_____
_____

Summary of Charges:

For Credit Card, Checking Account and Direct Billing, explain to the Customer the following:
OK Mr./Mrs. _____ the charges that will be applied to your credit card or checking account or direct billing today are:

Your recurring monthly charges consist of:
1) Unlimited LD or Special Pricing Plan: $_____
2) The Toll Free Emergency Calling A and Card for: $_____
3) Monthly internet access fee of: $_____
Your recurring monthly total charge is: $_____

Your one time charge consists of:
1) The Processing Fee for the 6.9 Plan of: $_____
2) Your Activation and Shipping Fee for the Pager $_____
3) The 10.95 per month Internet Access prepaid for 24 months which totals: $_____
4) An internet activation fee of: $_____
Your one time total charge is: $_____

The total amount to be charged to your credit card/checking account will be $_____ **Plus Taxes**

For Unlimited Calling Plan, say:
1. Now, Mr./Mrs. _____ each month you'll get your Connect Free statement for review seven days in advance of any charge or withdrawal.

For ConnectFREE 6.9 Cent Calling Plan, say:
2. Now, Mr./Mrs. _____ your 6.9 cent rechargable amount will get replenished whenever your account has only 20% left and your monthly statement will reflect all account detail.

For checking account only verify the following:

And just to confirm, for your information you may want to write this down.
1. The name on the account that the charge will be withdrawn from each month is: _____. Correct?
3. And, Mr./Mrs. _____, monthly ongoing automatic payments will be deducted from your account for as long as you remain on our service? OK? (Requires a yes or no response.)

Note: Validate now for credit authorization. You must get credit card or checking account authorization before order is processed.

ORDER CONFIRMATION

Pager Verification
(Stand Alone)

FINAL VERSION
Revised 2/12/99 12:30 pm

Closing:
Now, just for identification purposes (and to protect your account from any unauthorized changes) can I please have your Social Security number?

☐☐☐-☐☐-☐☐☐☐

If customer refuses say: Ok, Sir/Ma'am may I have just the last 4 digits of your Social Security number?

☐☐☐☐

If customer still refuses says: I understand how you feel Sir/Ma'am remember it's just for your protection. May I have the month and day of your birthday?

☐☐-☐☐

As a reminder, Mr./Ms. _____, your ConnectFREE charges will appear on your next (choose one: credit card/bank/direct billing) account statement, with our guarantee that if you are ever dissatisfied within your first 30 days of service, 100% of your domestic charges will be credited to you, no questions asked. I'd like to now thank you for calling in today and before I go is there any other way I may service you? O.K. Thanks and Welcome to ConnectFree!

Programming note: The computer must call up either "credit card", "bank", or "direct billing" in the last paragraph

ORDER CONFIRMATION **Exit Upsell Verification** FINAL VERSION?

Revised 2/12/99 12:30 pm jas

Note: Press play and begin recording now! Just read and let the customer confirm that the information is correct.

Introduction:

O.K. now, I will be recording this call to insure accurate order entry of your ConnectFREE Services. As we discussed you will receive a written confirmation stating all your terms in writing. Should you have any questions after you review this information, just call our Customer Care Center for assistance. Now today is (Name of day, e.g., Monday), (Date: Month, day, year) and you have called to receive Connect Free:

Privacy Minder ☐ Pager ☐

Date: ☐☐ ☐☐ ☐☐

Now, Mr./Mrs. _____ your caller code from the ad is 6_____, correct? Great!

1. Now, do you have the authority to approve the ConnectFREE Services?

Privacy Minder: *Note:* If no Privacy Minder, skip

O.K. Mr./Ms. _____, I just want to confirm that you will be receiving your three FREE months of our Privacy Minder service. This service is absolutely FREE for the first 3 months to give you plenty of time to evaluate your new found peace. Then Privacy Minder continues to protect you from telemarketers at the annual rate of $39.95,** unless canceled.

O.K. Mr./Ms. _____, I just wanted to confirm that you'll be receiving a FREE Motorola/NEC Pager and one month of FREE unlimited paging.

With a one-time activation and shipping fee of only $29.95 and ongoing paging for just $9.95 per month. ***

Billing Data & Read Back

1. OK, now, your name is. ☐

And the home phone bill comes in your name, correct?

Note: If your customer is anyone other than the owner of the phone bill (or their spouse) you must ask: Now is there anyone else that needs to be involved in this decision besides yourself? (If Yes, you must get the other person's approval).

2. Your Main Telephone Number is: ☐☐☐ ☐☐☐ ☐☐☐☐

2a. The exact billing name we have for that number is:
Is that how the name appears on the local bill?
☐
Billing Name

3. And the daytime number we can reach you at is: ☐☐☐ ☐☐☐ ☐☐☐☐
Daytime number

***

ORDER CONFIRMATION **Exit Upsell Verification** FINAL VERSION 2
Revised 2/12/99 12:30 pm las

Note: Keep recording!

Payment Method:
Now Mr./Ms. _____, you did state that you would like to pay your PrivacyMinder service with a credit card or automatic checking or direct billing, correct?
(Requires a yes or no response)

NOTE: Just read and let the customer confirm that the information is correct.

BOX 1 If Credit Card Complete:	BOX 2 If Automatic Checking Complete:
Enter Card Type MasterCard ☐ Visa ☐ American Express ☐ Discover ☐ Diners Club ☐ And your account number is: ☐ And your expiration date is: ☐☐ ☐☐ And the cardholders name as it appears on the card is: ☐ *Note: If credit card name is different from the caller, say: And your relationship to the cardholder is:* ☐ *If card holder is not the spouse, offer automatic checking option. If no checking account – offer direct billing!* Combination: CC/Debit Card	And the name of your Bank is ☐ Now, sir/ma'am, I need your account number. Do you have a check handy? Ok, sir/ma'am, what's the check # on that check? ☐☐☐☐ Now, look at the bottom of that check, can you please give me your account #? ☐☐☐☐☐☐☐☐☐☐ Ok, please read off the other large group of numbers minus the check # - they should be the numbers in between the columns. ☐☐☐☐☐☐☐☐☐ Now, for your own record keeping, please void out that check. And the name on the account as it appears on the check: ☐ *Note: If checking account name is different from the caller, say: And your relationship to the person's name on the account is:* ☐ *If name on the checking account is not the spouse, offer credit card option. If no credit card – offer direct billing!*

BOX 3 If Direct Billing Complete
Now is your direct billing address the same as we discussed? yes no If no, get proper billing address:.

Pager:

Finally, as a preferred customer benefit, you're entitled to a FREE Motorola/NEC pager with one month of FREE unlimited paging! The pager is FREE as a customer reward with a one time activation and shipping fee of only $29.95! After your free month, the pager's yours to keep! You may continue unlimited paging for $9.95 per month conveniently billed to the same credit card/checking account you gave us, or cancel within 60 days without further obligation. Would you like one?

Note: If yes, respond: Is one enough? Pager Quantity: ☐

Summary of Charges

For Credit Card, Checking Account and Direct Billing, explain to the Customer the following:
OK Mr./Mrs. _____ the charges that will be applied to your credit card or checking account or direct billing today are:

Your recurring monthly charges consist of:
1) Unlimited LD for $_____
2) The Toll Free Emergency Calling # and Card for: $_____
Your recurring monthly total charge is: $_____

Your one time charge consists of:
1) The Processing Fee for 6.9 Plan of: $_____
2) Your Activation and Shipping Fee for the Pager: $_____
Your one time total charge is: $_____

The total amount to be charged to your credit card/checking account will be $_____ Plus Taxes

For Unlimited Calling Plan, say:
1. Now, Mr./Mrs. _____ each month you'll get your Connect Free statement for review seven days in advance of any charge or withdrawal.

For 6.9 Cent Calling Plan, say:
2. Now, Mr./Mrs. _____ your 6.9 cent minutes will get recharged whenever you need them and your monthly statement will reflect all account detail.

For checking account only verify the following:

And just to confirm, for your information you may want to write this down.

1. The name on the account that the charge will be withdrawn from is: _____. Correct?
2. And, Mr./Mrs. _____, you do understand that the monthly ongoing withdrawals will be deducted from your account for as long as you remain on our service? Correct?

Note: Process now for credit authorization. Must get credit card or checking account authorization before order is processed.

ORDER CONFIRMATION **Exit Upsell Verification** FINAL VERSION 9

Revised 2/12/99 12:30 pm las

As a reminder, Mr./Ms. _____, your ConnectFREE charges will appear on your next (choose one: credit card/bank/direct billing) account statement, with our guarantee that if you are ever dissatisfied within your first 30 days of service, 100% of your domestic charges will be credited to you, no questions asked. I'd like to now thank you for calling in today and before I go is there any other way I may service you? O.K. Thanks and Welcome to ConnectFree!

Programming note: The computer must call up either "credit card", "bank", or "direct billing" in the last paragraph

Attachment C

retraining purposes, and things of that nature. So there was a manager over that department as well.
And there was a manager over the pager department, and also -- let's see if I left anybody out. There was a manager over the order entry staff, the people who typed in the orders. I think I covered everybody.
Q. How many employees in total does MRP have?
A. I don't think I know exactly right now.
Q. Can you estimate?
A. Maybe 400.
Q. Has that number substantially changed since 1997?
A. Well, between then and now it changed substantially probably twice. Once was a slow but steady increase in employees, but then since the -- since the marketing activity has ceased, the amount has decreased.
Q. I'm sorry. So 400 are currently employed?
A. That is my guess, yes.
Q. And in 1997 approximately how many would have been employed? Or pre-July 1998, based on what you indicated earlier, you ceased telemarketing, and those employees were actually not your employees was my understanding?

A. That's right.
Q. So how does the cessation of providing telemarketing impact the number of employees that MRP actually has?
A. That number is impacted in a couple of departments. Number 1, with no new sales coming in, there's no quality assurance process. So if there's no tapes to review, there's no employees to review the tapes. So that number would decrease substantially. With no new orders coming in, there's no order entry staff, so that number also decreases substantially.
With no new customers being added, all that's really happened to the account base is it's -- it just begins to erode due to attrition. So the number of customer service representatives has gone down in proportion to the customer base becoming smaller.
And then also the -- what we call the Melco staff or the monitoring staff -- there's no sales to monitor, so there's no monitoring staff. So that would -- that would be the sum total of how our direct employees would be impacted by a marketing cessation.
Q. Now, you indicated that no new sales were coming in, so I want to make sure that I understand you correctly. Is it your testimony that the sole means by

which MRP obtains customers is through your telemarketing efforts?
A. You mean previously?
Q. I mean now. Or, yeah, previously and now.
A. Now there's no -- there's no method of obtaining customers because there's no sales, so --
Q. Well, I guess my question is are you saying there are -- why are you saying there are no sales? Why do you believe there are no sales?
MR. DIERCKS: Your Honor --
THE WITNESS: I don't understand the question.
MR. DIERCKS: I would put an objection on the record. I have no problem with him answering, but I don't want to waive this objection in the future. The question was put in terms of his belief as to why something was going on as opposed to a fact. I will let it go.
BY MS. FOX:
Q. I may not be being very clear, and I will try and rephrase it. Is it your testimony that MRP's sales of telemarketing -- of telecommunications service is exclusively tied to its telemarketing efforts?
A. For clarification, do you mean now or before we stopped marketing?

Q. Let's take either. Let's take before and let's take now.
A. Before marketing ceased, we -- I hope I understood your question -- we used outside telemarketers to solicit Minimum Rate Pricing service. That's what I'm saying.
Q. Were you obtaining any sales through any method other than the telemarketing efforts of those telemarketers?
A. The only other way that a customer would be obtained would be if a customer called up the customer service department and said I have another -- I have a summer home that I want to add or with a certain type of qualifications, if a person called up and said, My friend, John Doe is on Minimum Rate Pricing and he told me about it and I want to be on, then a person could come on through that way. But that would probably be like, you know, one hundredth of one percent. I mean the -- our sole marketing effort was through telemarketing.
Q. Thank you. I appreciate the answer. You indicated earlier that the date that you ceased providing any telemarketing strategy in Tennessee. Was the July 8th date relative to Tennessee?
A. I didn't specify Tennessee, but it was the

whole country, so Tennessee would be included.
Q. And how do you know that July 8th is the date?
A. Well, July 8th is the date that we notified the telemarketing agencies that we no longer were going to continue the MRP campaign. There were -- and I don't know if I should say this, because I don't know exactly the -- the exact date. There was one agency that had a contract that I think required a seven-day but it might have been a ten-day but it was some period after notice that they had to wind down because of the cost effect on them because -- so there was one agency that continued for the week after July 8th.
But the way I know that July 8th is the date is that's the date that we gave notice to the agencies that we weren't going to allow marketing on our behalf.
Q. So it's true that after July 8th there have been additional telemarketing calls made to consumers, including in the state of Tennessee?
A. There may have for about a week, yeah.
Q. Does MRP have any affiliates? I use the term "affiliate." Does MRP have a parent company? Let's start there.
A. Yes.

Q. What's the name of your parent company?
A. Minimum Rate Pricing is owned by a company called Parcel Consultants, Incorporated.
Q. And are there any sister companies to Minimum Rate Pricing? Does Parcel own other companies?
A. No.
DIRECTOR GREER: Your answer to her question then is that MRP is the only subsidiary of Parcel Consultants, Incorporated?
THE WITNESS: Correct.
BY MS. FOX:
Q. Are there any other companies owned by Minimum Rate Pricing?
A. No.
Q. Where is Minimum Rate Pricing physically located -- their office physically located?
A. 150 Commerce Road, Cedar Grove, New Jersey.
Q. And are the employees to which you earlier referred located within that -- would they have been located within that physical location?
A. Yes, with the exception of the quality assurance department. They were about a mile down the road in Wayne, New Jersey.
Q. Where is the physical location of the company who provides telemarketing -- provided

am placing an order as long as I have this review period and I'm going to be able to see it in writing before the change takes place.

So I think I would really like for the record to differentiate between a -- a blatant, Don't do anything, don't put me down for anything, I'm not verifying anything, just send me a brochure versus, Yeah, I'll proceed and I'll place an order as long as I have a chance to review it before the actual carrier change takes place. I just wanted to clarify that difference.

DIRECTOR GREER: Well, in two other places on the same page -- now, you are assuming that everybody understands you're talking about you're soliciting them for long distance business, but in two other places on here you say, I am offering you 60 free minutes of phone service, and again -- and that's under I am happy with my current long distance carrier. And down at the bottom under, "I don't make long distance calls," you state again that you are offering 60 minutes of free telephone service.

I'm going to have to tell you that would indicate to me I've got 60 minutes of free telephone service, whether it's local or long distance. You don't differentiate between a local and long

distance call. You can assume you are offering long distance service because you know what you're selling, but an unknowledgeable consumer cannot assume that. You are offering 60 minutes of free telephone service, and you don't have the authority to offer free -- 60 minutes of free telephone service. That's the local -- their local carrier offering that. I think that's gross misrepresentation. You are welcome to respond to it.

THE WITNESS: Well, I mean the first question -- customer question that you pointed out, I am happy with my current long distance carrier, if is raised by the consumer, they obviously know that we're talking about a solicitation to switch long distance service.

DIRECTOR GREER: But then you go further to say, "But I am offering you 60 free minutes of phone service...." You don't say long distance service; phone service. I'm going to tell you there are a lot of people out there that don't know as much about the telephone business as you and I think they do and certainly don't know as much about it as you do.

THE WITNESS: That's -- that's probably true, but we still are offering 60 free minutes, so I don't think the statement is untrue

because we are -- we did offer 60 free minutes and sent them a coupon that said they could take advantage of that.

DIRECTOR GREER: Mr. Williams.

BY MR. WILLIAMS:

Q. Following up on that a little bit, as I understand your response, and you can -- let me ask you a question. Do you -- it is your position on behalf of MRP that if a customer tells you that I just need to see it in writing before I make a decision that they have to say something else -- they have to be adamant about not seeing it in writing in any, way, shape, manner, and that you not make a shape before it -- you won't follow through with the process and switch?

MR. DIERCKS: Object to the question. It's a compound question.

CHAIRMAN MALONE: Overruled.

THE WITNESS: It's our position that a customer that asks this question or makes this comment is going to receive a response, and if they continue through the entire verification process, then they have an understanding that their carrier is being changed and they are going to have an opportunity to look at written information prior to the carrier change and that they have a cancellation period.

BY MR. WILLIAMS:

Q. So what MRP's position is is that they disregard the statement of the consumer in favor of them just answering the other questions in the verification process? They would disregard the clear language of the consumer that before I make a decision I want to see it in writing? They just disregard that. And if the consumer answers the other questions in the verification process, then they are switched anyway?

A. No. That's not -- I would -- it's not my position that it's disregarded. The -- a customer's comment is taken in the context of where they are in the process, and there is a huge difference between a person saying, This sounds great. I want it. I just want to make sure that I get some written material on it before the change actually goes into place and somebody that's just saying, Don't ask me questions. Don't sign me up. Don't do anything. I don't want anything. You are free to send me literature. There's a world of difference between those two.

So comments are not disregarded. They are -- we've provided scripted answers to the -- you know, to what we felt addressed the customer's concerns the most properly, and then the customer is obviously free to continue or not to continue.

Q. What is flat rate -- flat rate pricing plan? Have you ever heard of that?

A. Well, I mean, we changed in the beginning of January to a flat rate offer.

Q. Is flat rate pricing plan a company or anything?

A. Well, MRP changed in the beginning of this year from a percentage off of AT&T, MCI, Sprint -- a discounted plan to a 15 cent, 12 cent, 11 cent, 10 cent. So MRP changed its pricing plan to a simplified flat rate.

MR. WILLIAMS: I only have a few more questions, I think.

DIRECTOR GREER: Mr. Williams, if you're going to leave that area, I want to go back to this sheet for just a minute while you're preparing for the next question. Mr. Keena, you said to me they fully understand they are getting long distance calls, but under one of these questions it says I don't make long distance calls. That's fine, but you are still going to get 60 minutes of free telephone service.

Now, these people are telling you they don't make long distance calls and yet you're still offering them 60 minutes of free telephone service. I will just contend that I think the offer of 60 minutes

of free telephone service is a misleading statement.

THE WITNESS: Can I respond?

DIRECTOR GREER: Absolutely. You can also tell me what "15/12/8.9 CPM" means.

THE WITNESS: I'll be happy to.

DIRECTOR GREER: Because I guarantee if I don't know, there's not many customers out there that know what it means.

THE WITNESS: The written response to "I don't make long distance calls" is, "That's fine sir/ma'am whenever you do make a call" -- because generally I don't make long distance calls in the context of what the person is saying is that they are not a heavy long distance user, and generally it's not I have never made a long distance call and I'm never going to. So the answer is whenever you do make a call, you will automatically be receiving a -- CPM stands for cents per minute, so that's 15 and the one that the customer is being offered would be selected. So either 15, 12, or 8.9 cents per minute. That's what that stands for.

BY MR. WILLIAMS:

Q. I'm showing you what counsel has reviewed and indicates it's the continuing response to Discovery Request No. 13 which asks what jurisdictions have

actually speak with the customer prior to the customer signing up for the service?
A. I'm sorry. Could you repeat or clarify?
Q. Yeah. All I'm trying to get at is a distinction between your various levels of employees. We indicated in some of our discovery responses it was unclear as to whether MRP had employees who did these various things, and so now that you've indicated that you have a number of employees who do -- have a number of different functions, I'm trying to figure out who does what?
A. Okay.
Q. So you have a group of people who do telemarketing, but they are not employed by Minimum Rate Pricing and their offices are external to the Minimum Rate Pricing employees' offices?
A. Right.
Q. You have people who provide quality assurance for Minimum Rate Pricing; correct?
A. Correct.
Q. And those people are located outside of the building where Minimum Rate Pricing's telemarketers telemarket; correct?
A. When they were employed, that is correct.
Q. And with respect to customer service, are

those employees located within the same physical location that the -- that Minimum Rate Pricing's customer service representatives are located?
A. I think --
Q. Did I say that twice?
A. I think you said are the customer service reps are located where the customer service reps are.
Q. I may have said it twice. Are the customer service representatives located in the same place where the quality assurance employees are located?
A. No. The customer service reps are in the same facility as all the other employees.
Q. Okay. Now, what types of -- you indicated in your testimony that the customer service department addresses issues relating to customer service and inquiries from customers. What kind of customer inquiries?
A. That would vary greatly. You want me to give you a few?
Q. Please.
A. It could be anywhere from, you know, I make a lot of calls to, you know, Uganda, can I have a special -- is there any special rate plan for people who have heavy calling on an international basis? It could be, I'm having trouble working my calling card.

I don't know how my pager works. I don't think I made this call to Duluth, Minnesota. It can be a whole host of things.
Q. I'm a little confused because we were speaking earlier about the extent to which your sales are tied to any calls, and now you indicate that you did receive -- you do receive some calls and your customer service department funnels or fields, if you will, through some calls that inquire about the ability of MRP to provide service to a customer; is that correct? A potentially new customer.
A. I was referring in my previous comment to people who were already on the service, not to people prior to being on the service.
Q. So people phoning MRP is not a means by which MRP used -- MRP obtains new customers?
A. No. With the small exception of the thing that I mentioned earlier where in some very, very rare cases a customer -- a new person might call up and say, John Smith is an MRP customer and he referred me to you. Once we confirm that John Smith is indeed an MRP customer and it was a legitimate referral, then that call would be taken by a customer service rep, but it was not a -- it happens as it happens. It's not really a -- you know, it wasn't a sales or marketing means for

us to obtain customers. It was just, hey, these people are calling up saying that their friends referred them, what do we do?
Q. Does MRP believe that name recognition is important in the industry?
A. I don't know what you mean.
Q. Does MRP believe that having people throughout the United States and in other locations know who MRP is is important to its marketing efforts?
A. I think that we -- we -- we kind of resolved ourself long ago that without a multibillion dollar ad campaign, we're not going to be able to obtain name recognition, and because our sole method of marketing was individual solicitations, we never -- we never really thought that there was ever a chance of obtaining that name recognition because we didn't really have the means or the wherewithal to get our name out to the masses.
Q. How many customer complaints did MRP receive in 1997?
A. I don't know.
Q. Does MRP keep those records?
A. Could you define what you mean by a complaint?
Q. Let me change the word to inquiries. If,

as you indicated, people can contact MRP and you have a customer service department for the purpose of receiving those calls, what happens when those calls come to MRP? Is there a log of the call is my question?
A. The practice is as follows: The customer service rep would take the call and handle the call to the best of their ability, and then at the end of the call there's a function in the customer service computer database where the customer service rep is instructed to insert any notes, regardless of what the nature of the call was. Even if it was the simplist list of inquiries, the policy was still for the customer service rep to make notes of that telephone call. So there would be the date, the time would show up, the name of the customer service representative who took the call, and then generally a brief description of what transpired on the call.
DIRECTOR GREER: Ms. Fox, have you left the subject of marketing for the time being? Because if you have, I would like to go back and ask a couple of questions before we get completely off that.
MS. FOX: I was going to get back to it, but go right ahead.
DIRECTOR GREER: Let me ask you a

question, Mr. Keena. What is your company's present business plan? Are you willing to disclose that to us? What is the plan for your company?
THE WITNESS: Right now we're trying to see if we can survive, actually, as attrition takes its toll. We have -- we're currently kind of toying with a couple of different ideas, which I guess is more of -- it couldn't do me any harm to tell you. We have some ideas about maybe getting into some aspect of an Internet business, maybe providing -- being an Internet service provider. Fortunately for us, a WorldCom division who we have a contract with, Uninet, is probably the largest backbone provider of Internet service. So it would be -- it would be probably -- we probably might be able to get a pretty good deal on that basis.
We've toyed with some idea about getting back into the long distance business, maybe through a mailing advertising campaign which would produce calls in, inbound calls where the person would affirmatively call us saying, hey, I saw your ad, I want your service. But nothing really definitive right now.
DIRECTOR GREER: The reason I asked the question is I have been in business long enough to

know that you can't stay in business if your customer base continues to erode and you've discontinued marketing. My question directly is what's to prevent MRP from allowing its customer base to continue to erode to the point that all of these hearings that you have gone through throughout the country have become relatively meaningless because you would absolutely be unable to meet any obligations that might be assessed by any of the regulatory authorities around the country?

THE WITNESS: Well, to answer your question two ways, I think one thing that is preventing that from happening is our sheer, you know, desire to want to stay in business. I'm 33 years old with two kids and I have got a long -- a lot of years ahead of me to provide for my family. So, I mean, we have no incentive to just let the base of accounts erode.

But in regards to meeting obligations, we still have a fairly sizable base of accounts that we are doing our -- giving our best effort to make sure stay satisfied and stay on the network as long as possible. So I don't think that we would have a problem meeting obligations in that regard.

But going back to the core of your question, I just think that the sheer need to

survive -- I mean, I've been with the company 11 years and I have a lot of time and effort in, and I don't think that anyone that has been around for any length of time has a desire to just wash their hands of the thing and walk away.

DIRECTOR GREER: Has your company paid any fines thus far?

MR. DIERCKS: Your Honor, I think --

DIRECTOR GREER: He either knows or he doesn't know. The answer is yes or no, and then he is free to explain.

THE WITNESS: The reason why I'm hesitating is I don't know if it was technically classified as a fine, but we have in the settlement with the 20 state attorneys general -- we have made two payments on that settlement, yes.

DIRECTOR GREER: Well --

CHAIRMAN MALONE: Are there any states where you were assessed a penalty, fine, or to pay under any settlement agreement that were not a part of that 20-state settlement?

THE WITNESS: There was the -- the only other one that I remember was about two years ago and that was a case where one of our telemarketers had inadvertently called a consumer in the state of Oregon.

And Oregon happens to have a -- what they call a "May I Continue Law," which says that -- I believe it's in the first 30 seconds of the solicitation, you have to ask the person may I continue and receive a positive answer, and our telemarketer allegedly did not do that and we paid a -- I'm going to say a $10,000 fine but it might have been 15,000. I'm not sure.

CHAIRMAN MALONE: Has MRP been decertified in any states because of slamming complaints?

THE WITNESS: We were decertified in the state of Wisconsin. I don't know if I could say that it was specifically for slamming complaints, but that was definitely one aspect.

CHAIRMAN MALONE: Were there any fines assessed in connection with that?

THE WITNESS: No, sir.

CHAIRMAN MALONE: MRP has not been decertified in any other state other than Wisconsin?

THE WITNESS: Not decertified. In Georgia we had a temporary certificate, and when it expired, the commission decided not to renew it, but it wasn't actually a decertification.

CHAIRMAN MALONE: Why did they not renew it?

THE WITNESS: I don't think they really said.

CHAIRMAN MALONE: Were there any complaints pending against MRP at the time in Georgia?

THE WITNESS: We had complaints and we had gone down for several meetings, and I think the decision not to renew kind of came as a surprise to us because when we had a meeting, the staff had said if you just supply us with a monthly report of the activities and complaint resolution, which we did every month during the temporary certificate, and then without any other meetings or any other communication they just decided not to -- not to renew it. So there had been some previous discussions and some requests by the staff to submit some materials on a monthly basis, which was done, and then for -- I mean, obviously, they don't have to answer to us. They have their own reasons for not renewing. They just decided not to.

CHAIRMAN MALONE: So they didn't issue an order stating their reasons?

THE WITNESS: I think they -- they sent out some notice that said on such and such a date -- I can't remember the exact date. It was sometime in July of 1998 -- the temporary certificate of Minimum Rate Pricing expired and the commission

is -- has decided not to renew.

DIRECTOR GREER: Well, to follow up on that line, in Alabama, Florida, and South Carolina, you had -- you indicated in your discovery response that we received in here on October 23rd that you were aware of investigations. What's been the outcome of those three?

THE WITNESS: I'm sorry. Can you name the states again?

DIRECTOR GREER: Alabama, Florida, and South Carolina.

THE WITNESS: Currently there's still open show cause orders in each of those three states, and we've been -- we've had several meetings, myself and counsel, in the various states, and there isn't any formal resolution.

DIRECTOR GREER: There's no fine in the state of Florida?

THE WITNESS: No. I think that they -- they -- in the show cause I think they put a number in there, but it's not finalized.

DIRECTOR GREER: I think my point goes to the point that at some point a business decision is reached that you continue to fight all these causes in 20 states in one issue and five or six states in

another, at some point it becomes not economically feasible to continue to fight, and, you know, there's -- Ms. Fox asked you if you had any affiliates, and I take it that you answered that question honestly. But there would be nothing to prevent you from transferring these customers to another affiliate and bankrupting Minimum Rate Pricing and leave all these 25 to 30 states that have actions against you sitting there holding the bag with nothing to compensate the consumers or penalties would be virtually meaningless.

And I -- what brought all this up was your comment that you have stopped marketing throughout the country, and you can't continue to stay in business very long if you're not marketing to your customers, and I would like for you to comment on that.

THE WITNESS: Well, I think that it's understood by the upper management of our company that there -- that we have to do something. I think that one of the things that is working against us is that we have some of these issues still outstanding, this one that we're presently in, other ones that you mentioned, Florida, Alabama, and South Carolina. And it's our first priority to make sure that those things are resolved to everyone's satisfaction because, as you have stated, I guess there does come a point where it

doesn't become economically feasible to fight and we're just not in the position if we ever are planning on marketing again in any fashion, which we obviously are, we can't just -- we can't just stop fighting and, you know, let's say, hey, you folks, okay, you're out of Tennessee and we're out of here and we're out of here. You start running out of states kind of fast.

So we have -- we have kind of bitten off on the fact that we're going to have to, you know, go through these proceedings and where there's fines issued, you know, to pay them to kind of show, you know, we're somebody who has planned to be in business for the long haul from the very beginning. We have always tried to do things right, and we're hopeful that that will be -- that the evidence will bear that out so we can kind of move on and be able to concentrate on things that are really going to make us a going concern.

DIRECTOR GREER: Wouldn't a simpler plan to be that once you had these 25 to 30 states filing complaints simply change your marketing plan to a marketing plan that would have been more acceptable that would have left you less open to criticism?

THE WITNESS: I guess not knowing what that plan would be and how any other plan would have

been viewed by other -- you know, by folks such as yourself, I mean, it's hard in our position to --

DIRECTOR GREER: Mr. Keena, I'm sorry to interrupt that, but I have a problem with that answer. We have probably 200 companies that are certified in this state, and we have very few complaints from most of them. Most of them have pretty good marketing plans I would think that seem to be acceptable to both the attorney general's office and to this Agency. I think that there are other companies who have set a pretty good record marketing their products to the public, and most of them do it by telephone. I get them at home every night and most of the time I refuse.

But the fact is that I don't find that their marketing has caused the concerns in this state that your company has, and it seems to me that as opposed to letting your customer base erode and virtually leaving the consumers out there who have filed complaints holding the bag, that the reasonable alternative would be to try to find out what other companies are doing and file a more positive marketing plan. I don't think -- our Agency has never been in the business or had a desire to put anybody out of business. We simply want the consumers of the state of

Tennessee to be called upon to have competitive market choices, and, you know, it just looked to me like the simplest part of your business plan would be to come up with a more positive business plan. That's an editorial comment for whatever it's worth. You may comment or not.

THE WITNESS: I appreciate the comment, and I think -- you know, our cessation of marketing I think was indicative that we wanted to make sure that we weren't going to resume marketing without a plan that would be more widely accepted, and I mean we absolutely will not come back into the marketing business without a plan that we're quite sure is going to meet those objections.

CHAIRMAN MALONE: So have you read Mr. Roberson's testimony?

THE WITNESS: I have read his rebuttal to mine. I don't know if I read his.

CHAIRMAN MALONE: In his testimony he states that according to your -- I don't want to be redundant to Director Greer's question, but according to MRP's response to staff's discovery request, it appears that five states have decertified MRP; Alabama, Florida, Georgia, South Carolina, and Wisconsin. And you're saying that in Alabama, Florida, and South

Carolina investigations may be ongoing and so forth, but there's been no decertification?

THE WITNESS: That's correct.

BY MS. FOX:

Q. Just a point of clarification, with respect to all of the states where MRP has either been decertified or is currently undergoing agency review, all of those actions involve slamming allegations to some degree; correct?

A. Correct.

Q. And with respect to each of the -- each of the jurisdictions where decertification has been at issue, each of those areas are heavily concerned with slamming; is that correct?

A. I think there's only one, but, yes, that's correct.

Q. I want to be brief, but since we got off track, I will go out of order. This is a response to Discovery No. 13 that includes copies of various jurisdictions. I think you have it somewhere. I would like to have it marked. I believe the number would be 10.

CHAIRMAN MALONE: Marked for identification.

MS. FOX: Marked for identification

and we will move it in as an exhibit in just a moment.

(Exhibit 10 marked.)

BY MS. FOX:

Q. Mr. Keena, do you recognize the response? Do you recognize these documents?

A. I would say I'm familiar with most of it.

Q. Would you agree that if there are documents that reflect what happened in various jurisdictions concerning Minimum Rate Pricing, then that they are what they are and they say what they say?

A. I don't think I know what you mean.

Q. Basically, what I'm asking is these are documents that are from other jurisdictions that were provided to our Agency in response to a request that asked about enforcement action that had been taken against Minimum Rate Pricing, and this was information that was supplied.

And I want to ask you, one, if you're familiar with what this is, and, two, if you have had any additions or corrections to this material since it was filed so that we are very clear that the Agency has at its disposal all of the documents in the record that relate to action that's been taken by Minimum Rate Pricing?

A. I don't know if I could say definitively at

this second, but it looks like it's fairly complete.

MS. FOX: Well, Mr. Chairman, I guess since we have no way of knowing whether any additional action has been taken, I would just like to ask if we could get just clarification that if there are any additional materials -- if he's not able to say and he's their witness, then somebody needs to make sure that they are able to say and that they supply any additional information if there is any.

DIRECTOR KYLE: When was the last time that our Agency checked, for example, in Georgia? I just need to turn back there. Commissioner Baker had signed an order I think it was in July. I could be wrong. September 16th Commissioner Baker wrote that the certificate of authority, I believe, has been revoked. That was September.

And when is the last time this Agency has checked to see if anything further has happened in any of these commissions? I just use this as an example. I mean, the reconsideration rights and so forth and that they have reapplied, any of those?

MS. FOX: I appreciate your concern. We honestly haven't asked. It's the responsibility of the companies to supply us with what's happening in the other jurisdictions and keep us apprised as changes

Attachment F

U.S. Department of Justice

Civil Division

JACK KAUFMAN, TRIAL ATTORNEY

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Washington, D.C. 20530

April 1, 1999

By First Class Mail

TO: SEE ATTACHED MAILING LIST

Re: Parcel Consultants, Inc., Case No. 99-32133; National Tele-Communications, Inc., Case No. 99-32135; Minimum Rate Pricing, Inc., Case No. 99-32136 (D.N.J.)

Dear Counsel:

The United States Department of Justice represents the Federal Communications Commission ("FCC") in the Minimum Rate Pricing ("MRP") bankruptcy proceeding pending in the District of New Jersey. As I discussed by telephone last week with New York State Assistant Attorney General Jill Sandford, the FCC is concerned that MRP abide by all terms and conditions of the FCC's December 16, 1998 "Order Adopting Consent Decree" and attached "Consent Decree" (collectively, the "Consent Decree"). In the event of non-compliance, the FCC intends, at the least, to take appropriate action consistent with its regulatory authority. Paragraph 9(a) of the Consent Decree, entitled "State Settlement," provides that "MRP shall comply with the requirements, which are not inconsistent with the requirements set forth in this Consent Decree, contained in the settlement MRP and numerous states signed on October 23, 1998" (the "October 23 Settlement"). In this regard, please inform me immediately if you believe that MRP either presently is not in compliance with October 23 Settlement, or if it fails in the future to comply with the October 23 Settlement.

Also, for your information, enclosed is a copy of the bankruptcy court's latest (to our knowledge) interim Order regarding the debtor's use of post-petition funding.

Please do not hesitate to telephone me if you have any questions or concerns.

Sincerely,

Jack Kaufman

cc: Stewart Block, Esq.

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UNITED STATES BANKRUPTCY COURT
DISTRICT OF NEW JERSEY

In re:	In Proceedings for Reorganization under Chapter 11 of the Bankruptcy Code
	Hon. Rosemary Gambardella, Chief Judge
PARCEL CONSULTANTS, INC., et al.,	Case Nos. 99-32133; 99-32135; and 99-32136
	Jointly Administered
Debtors.	INTERIM ORDER PURSUANT TO SECTIONS 363, AND 364(c)(1), (c)(2), AND (d)(1) OF THE BANKRUPTCY CODE AND RULE 4001 OF THE FEDERAL RULES OF BANKRUPTCY PROCEDURE AUTHORIZING DEBTORS TO SELL CERTAIN ACCOUNTS AND RECORDS, ENTER INTO CERTAIN BILLING AND COLLECTION ARRANGEMENT, OBTAIN INTERIM POST-PETITION FUNDING, GRANT SENIOR LIENS AND SUPER-PRIORITY ADMINISTRATIVE EXPENSE STATUS, AND ENTER INTO AGREEMENTS WITH OAN SERVICES, INC.

THIS MATTER came before the Court on March 19, 1999 upon the Motion of National Tele-Communications, Inc. ("NTC"), Parcel Consultants Inc. ("PCI"), and Minimum Rate Pricing, Inc. ("MRP"), (collectively the "Debtors") dated March 17, 1999, seeking, *inter alia*: (i) authority pursuant to Sections 363 and 364(c)(1), (c)(2) and (d)(1) of the United States Bankruptcy Code, 11

U.S.C. §§ 101, et seq. ("Bankruptcy Code") and Rules 4001 and 9014 of the Federal Rules of Bankruptcy Procedure ("the Bankruptcy Rules"), for MRP and the other Debtors, to obtain post-petition funding and incur debt by selling accounts and records to OAN Services, Inc ("OAN") up to the aggregate amount of $25,000,000.00 to be remitted by OAN to MRP on an interim basis to be secured by first priority security interests in and liens upon the following assets of the Debtors and the proceeds and products thereof, pursuant to Sections 364(c)(1), (c)(2) and (d)(1) of the Bankruptcy Code (collectively, the "Post-Petition Collateral"):

(a) all present and future accounts of the Debtors and the proceeds and products thereof, arising at any time, including all residual rights of the Debtors in any accounts or records sold to OAN;

(b) all reserves and all amounts at any time due from OAN to the Debtors under or in connection with any agreement with OAN;

(c) all of the Debtors' general intangibles;

(d) all of the Debtors' books and records;

(e) all of the Debtors' rights in and to all accounts, debts and other amounts payable to the Debtors by any billing and collection processor related to any accounts and records;

(f) all other assets and property of the Debtors of every nature, kind and description, whether now owned or hereafter acquired, including without limitation, all furniture, fixtures, leases, equipment, securities, and investment property, including without limitation, the Debtors' shares of stock in all wholly owned subsidiaries; and

(g) all current and future cash and noncash proceeds and products of the Debtors' assets and other rights arising from or by virtue of, or from the voluntary or involuntary sale or other disposition of, or collections with respect to, all or any part of the foregoing;

(ii) authority for MRP and the other Debtors to enter into an Account Purchase Agreement and Addendum No. 1 thereto with OAN (collectively, the "Funding Agreements"); (iii) authority for NTC on behalf of all the Debtors to enter into a Billing and Related Services Agreement and

Addendum No. 1 thereto with OAN (collectively, the "Billing and Related Services Agreements"); (iv) authority for PCI to enter into a Guaranty with OAN ("PCI Guaranty"); (v) authority for any Debtor who is a Permitted Affiliate as defined in the Funding Agreements and the Billing and Related Services Agrcements to enter into such agreements; (vi) approval of the terms and conditions of the Funding Agreements, Billing and Related Services Agreements, and the PCI Guaranty, as the same are or may be ratified, adopted and amended (collectively, the "OAN Agreements"); (vii) the granting to OAN of super-priority administrative claim status pursuant to Section 364(c)(1) of the Bankruptcy Code; and (viii) the setting of a final hearing on the Motion.

IT APPEARING, that at or prior to the hearing on the Motion, each of the parties identified on the Service List attached to the Motion received due notice of the Motion pursuant to Bankruptcy Rules 4001(c)(1), 4001(d)(1) and 1007(d); and it further

APPEARING, that the Debtors filed voluntary petitions for relief under chapter 11 of the Bankruptcy Code on February 26, 1999 (the "Petition Date") and are continuing in the management and possession of their businesses and properties as debtors-in-possession pursuant to Sections 1107 and 1108 of the Bankruptcy Code; and it further

APPEARING, that prior to the commencement of Debtors' chapter 11 cases, OAN regularly purchased records and accounts from and made other credit accommodations to MRP and the other Debtors pursuant to an Account Purchase Agreement dated October 1, 1995, as amended by that certain letter agreement dated December 22, 1997, and further regularly provided billing and related services to the Debtors pursuant to the terms of a Billing and Related Services Agreement dated August 1, 1997 (collectively, the "OAN Pre-Petition Agreements"); and it further

APPEARING, that the principal amount of all obligations, liabilities and indebtedness of MRP to OAN existing as of February 26, 1999 pursuant to the OAN Pre-Petition Agreements,

subject to credits arising from payments made and anticipated to be made by account debtors to OAN with respect to purchased accounts and records, was $17,394,954.78, together with interest accrued and accruing thereon and fees, commissions, costs, expenses and other charges accrued and accruing with respect thereto (collectively the "Pre-Petition Debt"), and that OAN asserts, and the Debtors agree, that OAN is fully secured pursuant to the OAN Pre-Petition Agreements and related financing statements by perfected and valid first priority security interests in and liens upon the following assets of the Debtors:

(a) all present and future accounts of the Debtors and the proceeds thereof, arising at any time, including all residual rights of the Debtors in any account or record sold to OAN;

(b) all reserves and all amounts at any time due from OAN to the Debtors under or in connection with any agreement with OAN;

(c) all of the Debtors' general intangibles;

(d) all of the Debtors' books and records;

(e) all of the Debtors' rights in and to all accounts, debts and other amounts payable to the Debtors by any billing and collection processor related to any account; and

(f) all current and future cash and noncash proceeds and other rights arising from or by virtue of, or from the voluntary or involuntary sale or other disposition of, or collections with respect to, all or any part of the foregoing;

(g) products of the foregoing;

(collectively, the "Pre-Petition Collateral"); and it further

APPEARING, that without the funding, other credit accommodations, and services proposed by the Motion to be provided by OAN, the Debtors will not have the funds necessary to pay their post-petition payroll, payroll taxes, service providers, inventory suppliers, overhead and other expenses necessary for the continued operation of the Debtors' businesses and the management

and preservation of Debtors' assets and properties; and it further

APPEARING, that the Debtors have requested that OAN continue to purchase accounts and records, and that the Debtors have requested that OAN continue to provide billing and collection and related services in order to provide funds to be used by the Debtors for their general operating, working capital and other business purposes in the ordinary course of the Debtors' businesses; and it further

APPEARING, that such funding, credit accommodations, and services are essential and will benefit the Debtors, their estates, creditors and equity security holders; and it further

APPEARING, that OAN is willing to enter into an agreement with MRP and the other Debtors to purchase post-petition accounts and records, and to enter into an agreement to provide post-petition billing and collection and related services to the Debtors, all on a continuing secured basis as more particularly described herein and subject to the terms and conditions contained herein; and it further

APPEARING, that the ability of Debtors to continue in business, remain viable entities and reorganize under chapter 11 of the Bankruptcy Code depends upon obtaining such funding, credit accommodations, and services from OAN; and it further

APPEARING, that the relief requested in the Motion is necessary, essential, reasonable and appropriate for the continued operation of Debtors' businesses and the management and preservation of their assets and properties; and it further

APPEARING, that the Debtors and OAN have negotiated the OAN Agreements in good faith and at arms-length; and it further

APPEARING, that this Court has jurisdiction to enter this Interim Order pursuant to 28 U.S.C. §§ 157(b)(2)(A), (D) and (M) and 1334;

NOW, THEREFORE, upon the Motion, the filings and pleadings in these cases, the record of the proceedings heretofore held before this Court with respect to the Motion and upon completion of the interim hearing, and after due deliberation and sufficient cause appearing therefor, the Court hereby finds as follows:

1. The Debtors are unable to obtain unsecured credit allowable under Section 503(b)(1) of the Bankruptcy Code, or pursuant to Sections 364(a) and (b) of the Bankruptcy Code.

2. No other source of interim funding exists on terms more favorable than those offered by OAN.

3. The Motion was filed on March 17, 1999 and the Debtors have provided actual notice of the Motion and the relief requested thereunder, the hearing in respect of the Motion and the terms of this Interim Order, whether by telephone, telecopy, overnight courier or by hand delivery to (i) the Office of the United States Trustee; (ii) OAN's attorneys; (iii) counsel for WorldCom Network Services, Inc. d/b/a/Wiltel ("WNSI"); (iv) counsel for Access Capital, Inc. ("Access"); (v) the twenty (20) largest unsecured creditors of each of the Debtors; and (vi) all parties in interest who have filed a Notice of Appearance in the Debtors' chapter 11 cases, all as more fully described in the Service List attached to the Motion. Sufficient and adequate notice of the Motion and the hearing with respect thereto has been given pursuant to Bankruptcy Rules 2002, 4001(c) and (d) and 9014 and Section 102(1) of the Bankruptcy Code as required by Sections 363, 364(c) and (d) of the Bankruptcy Code, and no further notice of, or hearing on the relief sought in the Motion is necessary or required.

4. The terms of the OAN Agreements, including, without limitation, any and all amendments thereto, pursuant to which post-petition funding, credit accommodations and services may be provided to any of the Debtors by OAN, have been negotiated in good faith and at arms

length as those terms are used in Sections 363(m) and 364(e) of the Bankruptcy Code, and are in the best interests of the Debtors, their estates, creditors and equity security holders.

5. Good, adequate and sufficient cause has been shown to justify the granting of the relief requested herein, and the immediate entry of this Interim Order.

6. WNSI and Access have asserted pre- and post-petition security interests in and liens upon the property of the Debtors' estates in which senior liens and security interests are held by and/or being granted to OAN.

7. ~~There is adequate protection for the interests of OAN,~~ WNSI, and Access consent to the entry of this O ~~on account of their pre- and post-petition liens on the property of the Debtors' estates on which such senior post-petition liens in favor of OAN are being granted.~~

8. As of March 17, 1999, no committee has been appointed in these cases pursuant to Section 1102.

IT IS on this 19th day of March, 1999,

ORDERED that the Motion is granted and approved as provided below; and it is further

ORDERED that good and sufficient notice of the Motion's request for the entry of this Interim Order and the hearing thereon has been provided in accordance with Sections 102(l), 363, 364(c)(1), (2) and (3) and 364(d)(1) of the Bankruptcy Code, Bankruptcy Rules 2002 and 4001, and any request for other and further notice shall be and is hereby dispensed with and waived; and it is further

ORDERED that the relief granted by this Court, pursuant to this Interim Order is necessary to avoid immediate and irreparable harm to Debtors' estates; and it is further

ORDERED that the Debtors are hereby immediately authorized and empowered to

enter into the OAN Agreements and to obtain post-petition funding, credit accommodations, and services from OAN pursuant thereto and pursuant to the terms of this Interim Order in such amount or amounts as may be made available from OAN in accordance with the terms of the OAN Agreements, *provided, however*, that pending the entry of a final order in respect of the Motion, such post-petition funding shall not exceed the aggregate amount of $25,000,000 to be remitted by OAN to MRP (inclusive of the Pre-Petition Debt) and it is further

ORDERED that the Debtors shall use the proceeds of the OAN funding for the payment of general operating and working capital purposes in the ordinary course of Debtors' businesses, including specifically, without limitation, the expenses authorized pursuant to that certain "Stipulation and Agreed Order By and Among Worldcom Network Services, Inc., OAN Services, Inc., Access Capital, Inc., and Minimum Rate Pricing, Inc., Parcel Consultants, Inc., and National Tele-Communications Services, Inc., as Debtors and Debtors-in-possession, (i) Authorizing and Conditioning Use of Cash Collateral and (ii) Granting Adequate Protection for Use of Collateral and Cash Collateral," and the Budget thereto attached as exhibit D-2, as the same may hereafter be revised, amended, modified, or supplemented (collectively, the "Interim Cash Collateral Order"); and it is further

ORDERED that the Debtors are authorized and directed to execute, deliver, perform, comply with, and expend such funds reasonably necessary to implement and effectuate the terms and covenants of, and pay all fees and charges associated with, the OAN Agreements. The OAN Agreements shall be substantially in the form annexed to the Motion as Exhibit 1-5. The terms and conditions of the OAN Agreements shall be deemed to be incorporated into the terms and conditions of this Interim Order and shall be sufficient and conclusive evidence of the funding arrangements, credit accommodations, and service agreements between the Debtors and OAN and of the Debtors'

assumption and adoption of the terms and conditions of the OAN Agreements, for all purposes, including the payment of all principal, interest, commissions, fees, service charges, and other fees and expenses, as more fully set forth in the OAN Agreements; and it is further

ORDERED that the Debtors have acknowledged and agreed and this Court hereby finds for all purposes in these cases, subject only to the rights of the Committee as hereinafter set forth below, that as of the Petition Date: (a) the OAN Pre-Petition Agreements are valid and binding agreements and obligations of the Debtors; (b) the principal amount of the Pre-Petition Debt due and payable to OAN by MRP, according to MRP's books and records as of February 26, 1999, consists of advances and other credit accommodations in the principal amount of approximately $17,394,954.78, together with interest accrued and accruing thereon and fees, commissions, costs, expenses, and other charges accrued and accruing with respect thereto, subject to credits arising from payments made and anticipated to be made by account debtors to OAN with respect to accounts and records purchased by OAN; and it is further

ORDERED that the Debtors have agreed and this Court hereby finds that the validity, perfection, and enforceability of OAN's pre-petition liens, or any other claims whatsoever against OAN are for all purposes, subject only to the rights of the Committee for a period of ~~sixty~~ ninety 90 (60) days from the date the Committee is appointed, to file a complaint pursuant to Bankruptcy Rule 7001, to invalidate, satisfy or subordinate the Pre-Petition Debt and/or to object to the extent, validity or perfection of OAN's pre-petition security interests and liens to the extent warranted or appropriate. If such complaint is not so timely filed, the Pre-Petition Debt and OAN's security interests and liens shall be recognized as valid, binding, allowed and in full force and effect with respect to all parties in these proceedings pursuant to Section 506(a) and (b) of the Bankruptcy Code; and it is further

ORDERED that to secure the prompt payment and performance of any and all post-petition

obligations, liabilities and indebtedness of any of the Debtors to OAN of whatever kind or nature or description pursuant to the OAN Agreements (collectively, the "Indebtedness"), OAN shall have and is hereby granted, effective as of the Petition Date, on and after the date of this Interim Order, valid and perfected first priority security interests and liens, superior to the liens and interests of any and all other creditors of the estates of the Debtors, including without limitation, the post-petition liens granted to OAN, WNSI, and Access pursuant to the Interim Cash Collateral Order, in and upon the assets of the Debtors, whether acquired prior to or after the Petition Date, including, without limitation, and by way of general description:

(a) all present and future accounts of the Debtors and the proceeds and products thereof, arising at any time, including all residual rights of the Debtors in any accounts or records sold to OAN;

(b) all reserves and all amounts at any time due from OAN to the Debtors under or in connection with any agreement with OAN;

(c) all of the Debtors' general intangibles;

(d) all of the Debtors' books and records;

(e) all of the Debtors' rights in and to all accounts, debts and other amounts payable to the Debtors by any billing and collection processor related to any accounts and records;

(f) all other assets and property of the Debtors of every nature, kind and description whether now owned or hereafter acquired, including without limitation, all furniture, fixtures, leases*, equipment, securities, and investment property, including without limitation, the Debtors' shares of stock in all wholly owned subsidiaries; and

(g) all current and future cash and noncash proceeds and products of the Debtors' assets and other rights arising from, or by virtue of, or from the voluntary or involuntary sale or other disposition of, or collections with respect to, all or any part of the foregoing;

(collectively, the "Collateral"**); and it is further

ORDERED that notwithstanding anything to the contrary set forth in this Interim

* (except for the real property lease concerning 150 Commerce Rd, Cedar Grove
OAN reserves the right to seek a lien on the Commerce Lease upon thirty (30) days prior written notice to Commerce Road Realty, LLC its counsel and Commerce reserves its rights to object to such reques

** provided, however, that nothing contained in this Interim Order or in any of the OAN Agreements or instrume executed in connection therewith shall be deemed to (i) grant OAN, World Cure, or Access, or any oth person or entity, directly or indirectly, any right, title or interest in to or under proper

Order, the security interests and liens hereby granted to OAN in and upon the Collateral shall not have priority over any valid, duly perfected liens held by equipment financers and lessors. The foregoing is without prejudice to the rights of the Debtors, the Committee or any other party in interest, including OAN, to object to the allowance of such equipment financers' and lessors' liens; and it is further

ORDERED that OAN is authorized and granted relief from the automatic stay under Section 363 of the Bankruptcy Code to set off and apply the proceeds of any Pre-Petition Collateral which it has collected or will collect post-petition, or any other amounts received by OAN in respect of the Pre-Petition Collateral, against the outstanding Pre-Petition Debt until such Pre-Petition Debt, and thereupon the Indebtedness, is paid and satisfied in full. In accordance with the OAN Agreements, OAN shall account periodically to the Debtors consistent with the terms of the OAN Agreements for such applications and setoffs; and it is further

ORDERED that this Interim Order shall be sufficient and conclusive evidence of the priority, perfection and validity of all of the senior security interests in and liens upon the property of the Debtors granted to OAN as set forth herein, without the necessity of filing, recording or serving any financing statements, or other documents which may otherwise be required under federal or state law in any jurisdiction or the taking of any other action to validate or perfect the security interests and liens granted to OAN in this Interim Order and the OAN Agreements. If OAN shall, in its discretion, elect for any reason, to file any such financing statements or other documents with respect to such security interests and liens, the Debtors are authorized and directed to execute, or cause to be executed, all such financing statements or other documents upon OAN's reasonable request, and the filing, recording or service thereof (as the case may be) of such financing statements and/or other documents shall be deemed to have been made at the time of and on the Petition Date;

and it is further

ORDERED that the Debtors are hereby authorized and directed to perform all acts and make all reasonable and necessary expenditures to execute, deliver and comply with the terms of such other documents, instruments, and agreements in addition to the above OAN Agreements, as OAN may reasonably require as evidence of and for the protection of the Indebtedness and the Collateral or which may be otherwise deemed necessary by OAN to effectuate the terms and conditions of this Interim Order and the OAN Agreements, each of such documents, instruments, and agreements being included in the definition of "OAN Agreements" contained herein; and it is further

ORDERED that OAN is authorized to collect the post-petition accounts and proceeds of the Debtors pursuant to the OAN Agreements and to apply such collections as set forth therein. In accordance with the OAN Agreements, OAN shall account periodically to the Debtors consistent with the terms of the OAN Agreements for such collections and applications of the Debtors' accounts and proceeds; and it is further

~~ORDERED that, pursuant to Sections 361 and 364(d)(1)(B) of the Bankruptcy Code,~~ as adequate ~~protection~~ for the security interests and liens asserted by Access ~~in~~ certain of the assets of NTC and PCI, which pursuant ~~to this Interim Order~~ are subordinated to the security interests and liens granted herein to OAN, MRP is authorized and ~~directed to make~~ periodic payments to Access ~~in the amount of $30,000.00 per week commencing on March 22, 1999; and it is further~~

ORDERED that for all Indebtedness of the Debtors to OAN, and in addition to the foregoing, OAN is granted an allowed superpriority administrative claim in accordance with Section 364(c)(1) of the Bankruptcy Code having priority in right of payment over any and all other obligations, liabilities and indebtedness of the Debtors, now in existence or hereafter incurred by the

* Notwithstanding anything herein to the contrary: (i) OAN is not presently receiving a lien or superpriority claim on avoidance actions under Chapter 5 of the Bankruptcy Code; and (ii) Commerce Road Realty LLC reserves all rights to assert claims and rights under Section 506(c) of the Bankruptcy Code

at OAN :serves e right to ek such lief in the ture.

Debtors and over any and all administrative expenses or priority claims of the kind specified in, or ordered pursuant to, Sections 326, 330, 331, 503(b), 506(c) or 507(b) of the Bankruptcy Code, except for (i) quarterly fees which may be incurred pursuant to 28 U.S.C. § 1930(a)(6) ("Trustee's Fees"); and (ii) Court-approved fees and expenses of professionals employed by the Debtors and the Committee pursuant to Sections 327 and 1103 of the Bankruptcy Code ("Professional Fees"); *provided, however*, that OAN shall not be responsible for the payment or reimbursement of any fees or disbursements of the Debtors or the Committee incurred in connection with the assertion or joinder in any claim, counter-claim, action, proceeding, application, motion, objection, defense or other contested matter, the purpose of which is to seek any order, judgment, determination or similar relief invalidating, setting aside, avoiding, subordinating, in whole or in part, the Pre-Petition Debt, the Indebtedness or OAN's liens and security interests in any of the Collateral, or otherwise challenging or contesting any aspect of the OAN Pre-Petition Agreements, OAN's pre-petition relationship with any of the Debtors, or any payments received by OAN pursuant to the OAN Agreements or OAN's pre-petition relationship with the Debtors; and it is further

ORDERED that OAN's security interests in and liens upon the Collateral and super-priority administrative expense claim shall be subordinate only to:

(a) Trustee's Fees paid quarterly when due; and

(b) any Professional Fees incurred prior to the expiration of the notice period after an Event of Default (defined below) which remain unpaid at that time**; and it is further

ORDERED that except for the Trustee's Fees and Professional Fees authorized above, and in consideration for same no costs or expenses of administration which have or may be incurred in the Debtors' chapter 11 cases pursuant to Section 506(c) of the Bankruptcy Code, or in any future proceedings or cases related hereto, shall be charged against OAN, its claims, or the Collateral, without the prior written

** such that upon receipt of a statement from a professional retained by the Court in

consent of OAN, and no such consent shall be implied from any other action, inaction or acquiescence by OAN and no obligations incurred or payments or other transfers made by or on behalf of the Debtors on account of the funding arrangements with OAN pursuant to the OAN Agreements shall be avoidable or recoverable from OAN under Sections 547, 548, 549, 550, 553 or any other provision of the Bankruptcy Code; and it is further

ORDERED that in the event of the occurrence of any of the following: (a) the failure of the Debtors to perform in any material respect any of their obligations pursuant to this Interim Order, (b) the occurrence of any default under or breach of the OAN Agreements which is not cured within any applicable cure or grace period provided for therein, (c) conversion of the Debtors' chapter 11 cases to cases under Chapter 7 of the Bankruptcy Code, (d) the appointment of a trustee pursuant to Section 1104(a)(1) or Section 1104(a)(2) of the Bankruptcy Code, in the Debtors' chapter 11 cases, (e) dismissal of any of the Debtors' chapter 11 cases, (f) the entry of any order modifying, reversing, revoking, staying, rescinding, vacating or amending this Interim Order without the express prior written consent of OAN (the foregoing being referred to in this Interim Order individually as an "Event of Default" and collectively as "Events of Default"); then (unless such Event of Default is specifically waived in writing by OAN) upon the occurrence of any of the foregoing after giving ~~three~~ five (5) business days notice in writing, served by overnight delivery service or telefax upon the Debtor, Debtors' Counsel, the Committee, counsel to the Committee, a trustee if appointed and the United States Trustee: (1) OAN shall be entitled to immediately terminate its obligations and duties under the OAN Agreements, and (2) OAN shall have no obligation to purchase accounts, lend or advance any funds to the Debtors or provide other financial accommodations or services to any of the Debtors upon or after the occurrence of an Event of Default and the expiration of ~~three~~ five (5) business days following the giving of notice as provided in this paragraph; provided, however, that such notice

requirements shall not apply to an Event of Default of the type specified in subparagraph (c), (d), (e) or (f) of this paragraph; and it is further

ORDERED that upon the payment in full of the Pre-Petition Debt and the Indebtedness to OAN, OAN and the Debtors shall each be released from any and all obligations pursuant to the terms of this Interim Order and/or the OAN Agreements; and it is further

ORDERED that OAN shall be entitled to the full protection of Sections 363(m) and 364(e) of the Bankruptcy Code with respect to accounts, records and assets purchased from the Debtors and the debts, obligations, liens, security interests and other rights created or authorized in this Interim Order in the event that this Interim Order or any authorization contained herein is vacated, reversed or modified on appeal or otherwise by any court of competent jurisdiction; and it is further

ORDERED that all post-petition funding, credit accommodations and services under the OAN Agreements are provided in reliance on this Interim Order and there shall not at any time be entered in the Debtors' chapter 11 cases any order which (a) authorizes the use of cash collateral of the Debtors in which OAN has an interest, or the sale, lease, or other disposition of property of the estates of the Debtors in which OAN has a lien or security interest, which is in any way inconsistent with the terms of this Interim Order (to the extent there is an inconsistency between such cash collateral authorization and this Interim Order, the provisions of this Interim Order shall govern); or (b) under Section 364 of the Bankruptcy Code authorizes the obtaining of credit or the incurring of indebtedness secured by a lien or security interest which is equal or senior in priority to any lien or security interest held by OAN, or which is entitled to priority administrative claim status which is equal or superior to that granted to OAN; and it is further

ORDERED that the provisions of this Interim Order and any actions taken pursuant hereto shall survive the entry of any order which may be entered converting the Debtors' chapter 11 cases

to chapter 7 cases, and the terms and provisions of this Interim Order as well as the priorities in payment, liens, and security interests granted pursuant to this Interim Order and the OAN Agreements shall continue in this or any superseding case under the Bankruptcy Code, and such priorities in payment, liens and security interests shall maintain their priority as provided by this Interim Order until the Pre-Petition Debt and the Indebtedness are indefeasibly paid in full and satisfied, and it is further

ORDERED that the provisions of this Interim Order shall inure to the benefit of the Debtors and OAN and shall be binding upon the Debtors and OAN and their respective successors and assigns, including any trustee or other fiduciary hereafter appointed as a legal representative of the Debtors or with respect to property of the estates of the Debtors, whether under Chapter 11 of the Bankruptcy Code or any subsequent chapter 7 cases, and shall also be binding upon all creditors of the Debtors and other parties in interest; and it is further

subject to the rights granted to the Committee herein,

ORDERED that if any or all of the provisions of this Interim Order are hereafter modified, vacated or stayed, such modification, vacation or stay shall not affect (a) the validity of any obligation, indebtedness or liability incurred by the Debtors to OAN prior to the effective date of such modification, vacation or stay, or (b) the validity or enforceability of any security interest, lien, or priority authorized or created hereby or pursuant to the OAN Agreements. Notwithstanding any such modification, vacation or stay, any indebtedness, obligations or liabilities incurred by the Debtors to OAN prior to the effective date of such modification, vacation or stay shall be governed in all respects by the original provisions of this Interim Order, and OAN shall be entitled to all the rights, remedies, privileges and benefits granted herein and pursuant to the OAN Agreements with respect to all such indebtedness, obligations or liabilities; and it is further

ORDERED that to the extent the terms and conditions of the OAN Agreements are in

conflict with the terms and conditions of this Interim Order, the terms and conditions of this Interim Order shall control; and it is further

ORDERED that the terms of the funding and other arrangements between the Debtors and OAN pursuant to the OAN Agreements and this Interim Order, were negotiated in good faith and at arms-length between the Debtors and OAN, and all funding, advances, account and record purchases, or other credit accommodations which are caused to be issued or made to the Debtors, or any one of them, by OAN pursuant to the OAN Agreements are deemed to have been extended in good faith, as the term is used in Sections 363(m) and 364(e) of the Bankruptcy Code, and shall be entitled to the full protection of Sections 363(m) and 364(e) of the Bankruptcy Code in the event that this Interim Order or any provision hereof is vacated, reversed or modified, on appeal or otherwise; and it is further

ORDERED that this matter is set for a final hearing at 11:00 o'clock A.m. on March 29 ,1999 ("Final Hearing"), in Courtroom 3E in the United States Bankruptcy Court for the District of New Jersey, Martin Luther King, Jr. Federal Building, 50 Walnut Street, Newark, New Jersey 07102; at which time any party-in-interest, may appear and state its objections, if any, to the funding, other credit arrangements, and service agreements of the Debtors. The parties identified on the Service List attached to the Motion shall immediately, and in no event later than March 29 1999, be mailed copies of this Interim Order or such written summary of this Interim Order as the Court may approve. Objections shall be in writing and shall be filed with the Clerk of the Bankruptcy Court with a copy served upon Debtor's counsel, the Office of the United States Trustee, parties who have requested notice in any of the cases, Counsel for the Committee, OAN's counsel, WNSI's counsel, and Access' counsel, so that such Objections are received on or before the close of business on March 25, 1999. Objections to any of the provisions of this Interim Order shall be deemed waived

unless filed and received on or before the close of business on the date specified above. Except as otherwise provided in this ~~paragraph~~ Interim Order, the terms of this Interim Order shall be valid and binding upon the Debtors, all creditors of the Debtors and all other parties in interest from and after the date of this Interim Order by this Court. In the event that this Court modifies any of the provisions of this Interim Order following such further hearing, such modifications shall not affect the rights and priorities of OAN pursuant to this Interim Order with respect to the Collateral and any portion of the Indebtedness which arises, or is incurred or is advanced prior to such modifications (or otherwise arising prior to such modifications), and this Interim Order shall remain in full force and effect except as specifically amended or modified at such final hearing.

BY THE COURT:

ROSEMARY GAMBARDELLA, CHIEF JUDGE
UNITED STATES BANKRUPTCY COURT

IT IS THE DIRECTION OF THIS COURT THAT THE SUCCESSFUL PARTY SERVE A FILED COPY OF THIS ORDER UPON ALL PARTIES TO THIS ACTION.

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107 F.3d 359
37 Collier Bankr.Cas.2d 950, 30 Bankr.Ct.Dec. 541, 1997 Fed.App. 65P
(Cite as: 107 F.3d 359)

In re Harry JAVENS and Joyce Javens, Debtors.
Harry JAVENS and Joyce Javens, Plaintiffs-Appellants,
v.
CITY OF HAZEL PARK and City of Royal Oak, Defendants-Appellees.

No. 95-1379.

United States Court of Appeals, Sixth Circuit.

Argued Oct. 3, 1996.

Decided Feb. 19, 1997.

Debtors filed bankruptcy petition when demolition by municipalities of debtors' three condemned buildings was imminent, invoking automatic stay to prevent destruction. Municipalities moved for determinations that demolition and related litigation was excepted from automatic stay. The Bankruptcy Court granted motions. Debtors moved for injunctive relief against one municipality and appealed orders granting motions. Debtors' case was subsequently dismissed. The United States District Court for the Eastern District of Michigan, Denise Page Hood, J., affirmed orders granting municipalities' motions. Debtors appealed. The Court of Appeals, Boggs, Circuit Judge, held that: (1) bankruptcy court was not required to inquire into circumstances of municipalities' proceedings before granting motions for determination that automatic stay did not apply, and (2) municipalities' actions in demolishing buildings were exercises of their police powers and excepted from automatic stay, pursuant to police powers exceptions.

Affirmed.

[1] BANKRUPTCY ⚿2361
51k2361
Filing petition under Bankruptcy Code creates legal barriers that repel, at least temporarily, many legal attacks against estate. Bankr.Code, 11 U.S.C.A. § 362(a).

[2] BANKRUPTCY ⚿2394.1
51k2394.1
Shield provided by automatic stay can repel actions by all entities, including governments. Bankr.Code, 11 U.S.C.A. § 362(a).

[3] BANKRUPTCY ⚿2467
51k2467
Dismissal of debtors' bankruptcy case did not affect appealability of orders recognizing that municipalities were excepted from automatic stay to enforce local building codes, inasmuch as actions for damages for willful violation of automatic stay survive dismissal. Bankr.Code, 11 U.S.C.A. § 362(h).

[3] BANKRUPTCY ⚿3766.1
51k3766.1
Dismissal of debtors' bankruptcy case did not affect appealability of orders recognizing that municipalities were excepted from automatic stay to enforce local building codes, inasmuch as actions for damages for willful violation of automatic stay survive dismissal. Bankr.Code, 11 U.S.C.A. § 362(h).

[4] BANKRUPTCY ⚿2467
51k2467
Action for damages for willful violation of automatic stay survives dismissal of case in bankruptcy. Bankr.Code, 11 U.S.C.A. § 362(h).

[5] BANKRUPTCY ⚿2057
51k2057
Inasmuch as dismissal of underlying bankruptcy case does not automatically strip federal court of residual jurisdiction to dispose of matters after case has been dismissed, exercise of such jurisdiction is left to sound discretion of trial court.

[6] BANKRUPTCY ⚿2402(1)
51k2402(1)
Bankruptcy court was not required to inquire into municipalities' determinations regarding condition of debtors' condemned buildings or validity of related state court proceedings before granting municipalities' motions for determination that automatic stay did not apply so as to prevent them from continuing litigation seeking demolition of condemned property, or carrying out such demolition, under police power exceptions to automatic stay. Bankr.Code, 11 U.S.C.A. § 362(b)(4, 5).

[7] BANKRUPTCY ⚿2371(1)

51k2371(1)
By creating exceptions from automatic stay for police and regulatory actions, Congress removed local regulation only from effect of automatic stay; it did not eliminate bankruptcy court's power to enjoin enforcement of local regulation which is shown to be used in bad faith. Bankr.Code, 11 U.S.C.A. § 362.

[7] BANKRUPTCY ⚷2402(1)
51k2402(1)
By creating exceptions from automatic stay for police and regulatory actions, Congress removed local regulation only from effect of automatic stay; it did not eliminate bankruptcy court's power to enjoin enforcement of local regulation which is shown to be used in bad faith. Bankr.Code, 11 U.S.C.A. § 362.

[8] BANKRUPTCY ⚷2371(1)
51k2371(1)
Although bankruptcy court may enjoin enforcement of local regulation that is shown to be used in bad faith, good faith of state and local officials should be presumed, only to be rebutted by particularized pleadings made after investigation, as required by rule, and proof of various forms of bad faith. Fed.Rules Bankr.Proc.Rule 9011, 11 U.S.C.A.

[9] BANKRUPTCY ⚷3781
51k3781
Even if appellate court were to treat as denials of debtors' motion for injunction bankruptcy court's orders excepting from automatic stay conduct by municipalities in demolishing debtors' condemned buildings under police and regulatory power, and to treat debtors' appeal from those orders as appeal of denial of motion for injunction, demolition of buildings rendered case moot.

[10] BANKRUPTCY ⚷2402(1)
51k2402(1)
Municipalities' actions in demolishing debtors' condemned buildings were exercises of municipalities' police powers, and thus excepted from automatic stay pursuant to police powers exception to provisions staying actions or enforcement of judgments against debtors, notwithstanding debtors' claim that actions had effect of controlling estate property and thus were not excepted from stay that arose under provision barring acts to exercise control over estate property, to which no exception applied; control provision upon which debtor relied did not apply to actions by governmental units to enforce police power. Bankr.Code, 11 U.S.C.A. § 362(a)(1-3), (b)(4).

[11] BANKRUPTCY ⚷2402(1)
51k2402(1)
Automatic stay did not arise under provision barring acts to exercise control over estate property so as to bar municipalities' conduct in demolishing debtors' condemned buildings, notwithstanding debtors' argument that exceptions for governmental use of police powers apply only to actions against debtors, while demolition orders being enforced were in rem, inasmuch as debtors' narrow interpretation was inconsistent with government's frequent use of in rem actions to enforce police and regulatory powers. Bankr.Code, 11 U.S.C.A. § 362(a)(1-3), (b)(4).

[12] BANKRUPTCY ⚷2394.1
51k2394.1
Automatic stay provision preventing commencement or continuation of action against debtor is not limited to in personam actions. Bankr.Code, 11 U.S.C.A. § 362(a)(1).

[13] BANKRUPTCY ⚷2402(1)
51k2402(1)
Exceptions to automatic stay permitting governmental unit to enforce its police or regulatory power are not intended to be limited to nondestructive exercises of governmental power. Bankr.Code, 11 U.S.C.A. § 362(b)(4, 5).

[14] BANKRUPTCY ⚷2467
51k2467
Even assuming that bankruptcy court erroneously determined that automatic stay did not apply so as to prevent municipalities from enforcing building and fire codes with regard to debtors' properties, debtors were not entitled to damages under statute providing for recovery for willful violation of automatic stay, inasmuch as municipalities could not be found to have willfully violated stays that bankruptcy court orders declared did not exist. Bankr.Code, 11 U.S.C.A. § 362(h).

*361 Hugh M. Davis, Jr. (argued and briefed), Hugh M. Davis, Jr., P.C., Detroit, MI, Harry Javens, Troy, MI, for Harry Javens, Joyce Javens.

Arnold J. Shifman, Philip H. Seymour (argued), Cooper, Shifman, Gabe, Quinn & Seymour, Royal

Oak, MI, Susan M. Lancaster (briefed), Sherman & Sherman, Bingham Farms, MI, for City of Hazel Park.

Lawrence A. Friedman (argued and briefed), Southfield, MI, for City of Royal Oak.

Before: KRUPANSKY, BOGGS, and SILER, Circuit Judges.

BOGGS, Circuit Judge.

Municipal authorities demolished three condemned buildings owned by Harry and Joyce Javens after they filed for bankruptcy. Should the automatic stay provisions of the Bankruptcy Code have required those authorities to desist from that exercise of local might? The district court and bankruptcy court below held that the Code did not prevent the Cities of Hazel Park and Royal Oak from sending bulldozers to enforce their laws. After careful consideration of the applicable provisions of the Code, we agree, and affirm the order of the district court.

I

In November 1989, four years and four months before the first building fell, the City of Hazel Park filed a complaint in Oakland County Circuit Court against the Javenses and others having an interest in the Blue Dot Building, an apartment house located at 20841 John R [sic] in that city. Hazel Park alleged that numerous building and fire code violations made the building a public nuisance and a danger to the public health, safety, and welfare. In July 1992, after two and a half years of procedural maneuvering, Javens (as we shall for simplicity call the plaintiffs) and Hazel Park entered into a consent judgment. Under its terms, the Blue Dot apartments were to be vacated; Hazel Park was to give Javens a definitive list of violations (it would fill five single-spaced pages); and Javens was to correct them all within one year after the premises were vacated.

A year and two months later, alleging that Javens had failed to comply with the consent judgment, Hazel Park filed a motion in the same state court for an order of immediate demolition. At a hearing on the motion, Javens claimed that he was unable to comply with the terms of the consent judgment because actions by Hazel Park employees had made it impossible for him to do so. Judge Nichols of the circuit court scheduled a bench *362 trial for December 3, 1993. Javens succeeded in obtaining two adjournments, and requested a third. That prompted Judge Nichols to cancel the bench trial. Hazel Park refiled its motion for an order of immediate demolition, and, at a hearing held on January 19, 1994, Judge Nichols granted the motion. However, certain persons having minor interests in the building had not been notified of the motion, so the city had to refile the motion and serve all the parties. At a new hearing on February 2, Judge Nichols entered an amended order to the same effect.

The Blue Dot Building was not the only Javens property that attracted Hazel Park's attention. In another Oakland County Circuit Court action, the city sought a declaratory action that thirteen other houses owned by Javens were nuisances per se, and that the buildings should either be brought up to code or demolished. One of these houses, at 422 East George Street, suffered damage in a fire in June 1993. Hazel Park sought an order of immediate demolition for that building. After several adjournments, Judge Schnelz of the circuit court personally inspected the building; he still had the motion under advisement as of February 2, 1994.

Meanwhile, in the nearby City of Royal Oak, a hearing officer for the city made determinations regarding yet another building owned by Javens, at 213 Euclid Street in that municipality. At a proceeding held on November 17, 1993, the officer found that

> [t]his house is in a seriously deteriorated condition requiring extensive building, plumbing, electrical and heating repairs. The owner, Mr. Javens, has had more than a year's time to repair the building but has made no apparent effort to comply with the orders of the Code Enforcement Division and the house continues to be an attractive nuisance, deteriorating the neighborhood.... THEREFORE, IT IS ORDERED that the house, all accessory buildings, and deteriorated fencing be demolished....

Five days later, Javens had the opportunity to show cause at a City Commission meeting why the order and findings of the hearing officer should not be

followed. Javens spoke at length, and asserted that Royal Oak police officers had prevented him from repairing the building by keeping him and contractors from entering the premises. Mr. Krupp, a Code Enforcement officer, also testified, as did Mr. Sutton, a neighbor on Euclid Street; both spoke of the building's decrepit condition. Javens complained of having received inadequate notice and information about the nature of the hearing. Nonetheless, at the close of the hearing, the commission voted unanimously to affirm the hearing officer's order of demolition, and to seek bids for the demolition of the house at 213 Euclid Street.

Thus, at the beginning of February 1994, two buildings owned by Javens faced imminent destruction, and the same fate seemed possible for a third. Javens sought sanctuary in the Bankruptcy Code. On February 2, 1994, the same day that Judge Nichols entered his amended order of immediate demolition for the Blue Dot Building, Javens filed a voluntary petition in United States Bankruptcy Court for the Eastern District of Michigan.

II

[1] Filing a petition under the Bankruptcy Code creates legal barriers that repel, at least temporarily, many legal attacks against the estate. The following statutory language creates these barriers:

> (a) Except as provided in subsection (b) of this section, a petition filed under section 301, 302, or 303 of this title, or an application filed under section 5(a)(3) of the Securities Investor Protection Act of 1970, operates as a stay, applicable to all entities, of--
>
> (1) the commencement or continuation, including the issuance or employment of process, of a judicial, administrative, or other action or proceeding against the debtor that was or could have been commenced before the commencement of the case under this title, or to recover a claim against the debtor that arose before the commencement of the case under this title;
>
> (2) the enforcement, against the debtor or against property of the estate, of a judgment obtained before the commencement of the case under this title;
>
> *363 (3) any act to obtain possession of property of the estate or of property from the estate or to exercise control over property of the estate;
>
> ...

11 U.S.C. § 362(a).

The legislative history of the Code explains the purpose of this protection:

> The automatic stay is one of the fundamental debtor protections provided by the bankruptcy laws. It gives the debtor a breathing spell from his creditors. It stops all collection efforts, all harassment, and all foreclosure actions. It permits the debtor to attempt a repayment or reorganization plan, or simply to be relieved of the financial pressures that drove him into bankruptcy.

H.R. Rep. 95-595, at 340 (1978), reprinted in 1978 U.S.C.C.A.N. 5787, 6296.

[2] The § 362(a) shield can repel actions by "all entities," including governments. As one court explained, "the legislative history is clear that, in general, this [section] was intended to extend to governmental entities as well as private ones." Penn Terra Ltd. v. Dep't of Envtl. Resources, 733 F.2d 267, 271 (3d Cir.1984).

Some governmental attacks on the estate, however, penetrate the barrier. Pursuant to 11 U.S.C. § 362(b), the filing of a petition does not operate as a stay:

> (4) under subsection (a)(1) of this section, of the commencement or continuation of an action or proceeding by a governmental unit to enforce such governmental unit's police or regulatory power;
>
> (5) under subsection (a)(2) of this section, of the enforcement of a judgment, other than a money judgment, obtained in an action or proceeding by a governmental unit to enforce such governmental unit's police or regulatory power;

As the legislative history of the Code explains, "[t]hus, where a governmental unit is suing a debtor to prevent or stop violation of fraud, environmental protection, consumer protection, safety, or similar police or regulatory laws, or attempting to fix damages for violation of such a law, the action or proceeding is not stayed under the automatic stay." S.Rep. No. 95-989, at 52 (1978), reprinted in 1978 U.S.C.C.A.N. 5787, 5838.

The Code provides for no similar exception from any stays automatically generated against the proceedings described in the other subsections of § 362(a), including subsection (a)(3). Against such

actions, the barriers are fully effective, unless and until overcome by a successful petition in the bankruptcy court for relief from the automatic stay. See 11 U.S.C. § 362(d).

III

Javens notified Hazel Park and Royal Oak of his bankruptcy filing, and invoked the Code's automatic stay provisions to save his condemned buildings from destruction. Hazel Park promptly filed a motion in the bankruptcy court "for a determination that the automatic stay of § 362(a) does not apply to the litigation initiated by the City of Hazel Park to correct building code violations or obtain orders permitting demolition of properties in which the debtors or debtors' estate may have an interest." In re Javens, No. 94- 41069-G (Bankr.E.D.Mich. March 15, 1994) (order exempting Hazel Park from automatic stay). Javens opposed the motion by proffering evidence that the Blue Dot Building was not in fact a danger to the public, and by arguing that the bankruptcy court should preserve the estate by recognizing the stay. Javens also moved for an injunction against the city's proceeding with the demolition, and for sanctions against the city for acts already committed: [FN1] he averred that Detroit Edison, at Hazel Park's behest, had cut off electrical service to the Blue Dot Building, resulting in frozen pipes and related damage.

> FN1. 11 U.S.C. § 362(h) provides that "[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."

The bankruptcy court granted Hazel Park's motion, holding that "[t]he automatic stay does not prevent government from the exercise of police or regulatory power.... Hazel Park's effort to require adherence to building codes or demolish property that may *364 pose a threat to the safety and health of the community is clearly within the police or regulatory power of government. The exercise of this power is not barred by the operation of 11 U.S. Section 362." The holding applied to both the demolition order already obtained, and the litigation under way against the second Hazel Park property. Ibid.

On that very day, March 15, 1994, Hazel Park razed the Blue Dot Building. With his eye, no doubt, on obtaining § 362(h) damages for that act, Javens promptly appealed to the district court the bankruptcy court's order declaring the stay inapplicable to Hazel Park.

In early May 1994, Royal Oak sought an order from the same bankruptcy court declaring its actions against 213 Euclid exempt from the § 362 automatic stay provisions. Javens claims that he was not personally served with notice of the hearing on the matter, learned of it less than twenty-four hours before it occurred, and was represented not by counsel but by Joyce Javens, his wife, who was "completely unprepared and unfamiliar with the proceedings." On May 10, the bankruptcy court entered an order declaring that "the City of Royal Oak [']s actions regarding 213 Euclid are in fact exempt from the automatic stay provisions of 11 USC 362." Javens frantically sought to obtain emergency injunctive relief in state court, but before Javens could succeed, the bulldozers arrived at 213 Euclid. As he had done with respect to the Hazel Park action, Javens appealed the bankruptcy court's order of exemption to the district court.

Hazel Park obtained an order from Judge Schnelz on May 20 to compel Javens to repair the building at 422 East George within ninety days. On September 7, 1994, Hazel Park apparently demonstrated to Judge Schnelz's satisfaction that Javens had not complied with the May 20 order, and secured an order of immediate demolition. So the third building fell.

[3][4][5] Meanwhile, the bankruptcy trustee moved on May 3, 1994 to dismiss Javens's bankruptcy petition for failure to proceed in proper prosecution of the case. The bankruptcy court granted that motion on May 12. Javens moved for reconsideration. After a variety of motions and hearings, the bankruptcy court confirmed its dismissal of the case on August 3, 1994. Javens did not appeal that dismissal to the district court. [FN2]

> FN2. We do not think that the dismissal of the case in bankruptcy affects the appealability of the orders recognizing the cities' exemption from the automatic stay. An action under § 362(h) for damages for willful violation of an automatic stay survives dismissal of the case in bankruptcy. See Price v. Rochford, 947 F.2d 829, 830-31 (7th

> Cir.1991). "Since dismissal of an underlying bankruptcy case does not automatically strip a federal court of residual jurisdiction to dispose of matters after the underlying bankruptcy case has been dismissed, exercise of such jurisdiction is left to the sound discretion of the trial court. In re Carraher, 971 F.2d 327, 328 (9th Cir.1992); In re Morris, 950 F.2d 1531, 1534 (11th Cir.1992); In re Smith, 866 F.2d 576, 580 (3d Cir.1989)." In re Lawson, 156 B.R. 43, 45 (9th Cir. BAP 1993).

Javens's appeals of the bankruptcy court's two exemption orders proceeded in district court. He sought a reversal of those orders, and remand for a determination of damages resulting from violation by the cities of the automatic stays.

The district court affirmed the bankruptcy court's orders of exemption, agreeing that "the automatic stay does not prevent government from the exercise of police or regulatory power," and holding that it was "axiomatic" that the cities' actions enforcing its building and fire codes "are related to matters of public safety and health, and thereby well within their respective police and regulatory powers." In re Javens, No. 94-CV-71142-DT (E.D.Mich. Feb. 28.1995).

Javens timely appealed to this court. He was represented by counsel in connection with the order exempting Hazel Park, but represented himself in the appeal of the order exempting Royal Oak. [FN3]

> FN3. Javens requested leave to participate in oral argument pro se, which we granted with respect to the Royal Oak order. Javens, who is not a lawyer, appeared before this court and argued capably.

IV

Javens has two main arguments:

(1) If Javens's bankruptcy petition caused an automatic stay to arise under *365 either § 362(a)(1) or (2), the corresponding exceptions did not apply, because the cities were not legitimately exercising their police or regulatory power.

(2) Javens's bankruptcy petition caused an automatic stay to arise under § 362(a)(3), for which there is no police-power exception.

The district court found that the cities' actions, taken pursuant to their building and fire codes, as measures in furtherance of the public health, safety and welfare, were classic exercises of the police power, and thus were excepted by § 362(b)(4) and (5). In support of this conclusion, the cities cite Smith-Goodson v. CitFed Mortgage Corp., 144 B.R. 72 (Bankr.S.D.Ohio 1992) (actions related to city housing, nuisance, and fireprevention ordinances by their very nature are related to the public safety and health, and hence are exercises of the police power exempt from the automatic stay; by contrast, governmental actions primarily having a pecuniary purpose are not so exempt).

Javens offers two arguments against this conclusion: (A) the cities' actions were not legitimately related to the public welfare, because the determinations that Javens's buildings were unsafe were bogus; and (B) the cities' actions were not exercises of their police power, because they were instead efforts to control the property of the estate.

A

[6] Javens's briefs, here and below, contain a litany of charges of unfair treatment at the hands of Hazel Park and Royal Oaks authorities, not to mention the Oakland County Circuit Court. The cities discriminated in their enforcement of the building codes, Javens says; they threw up obstacles to his compliance with the building codes; he received inadequate notice of proceedings; his evidence and legal arguments were ignored. Together, Javens claims, these affronts constituted a violation of due process which vitiated the determinations that the buildings were dangerous.

Those determinations were not just unfair, Javens argues, they were inaccurate. He supplied the bankruptcy court with a description of extensive repairs he said he had already made to the Blue Dot, supported by an affidavit of his repairman and a structural engineer. The actions of Hazel Park, he alleges, were not based on the real condition of his buildings, but were illegal, oppressive, discriminatory, and a violation of due process.

Javens argues that it was the duty of the bankruptcy court to consider these matters. "It was an abuse of discretion for the bankruptcy court not to inquire into the actual condition of the premises and the substance of the state court proceedings," he maintains in his brief. "[T]he bankruptcy court had

the power to determine that even the police power exemptions under 11 USC § 362(b)(4) and (5) can be stayed in the event that the actions of the governmental entities exercising their police power have been carried out in a discriminatory manner." [FN4]

FN4. In support of this proposition, Javens cites In re William Tell, II, Inc., 38 B.R. 327 (N.D.Ill.1983). In that case, however, the discriminatory governmental action (refusal to renew a liquor license) was enjoined by the bankruptcy court by reason of 11 U.S.C. § 525, which prohibits governmental units from discriminating against debtors or former debtors in the issuance of licenses and permits. Id. at 330. Javens does not allege, of course, that the cities sought to enforce their building codes as a manner of discriminating against him as a debtor.

Setting aside any assessment of our own of Javens's claims that the state court proceedings were invalid, and that their conclusions about the dangerousness of the buildings were erroneous, we think his argument that the bankruptcy court should have inquired into these determinations before recognizing an exception to the automatic stay is foreclosed by the Supreme Court's decision in Board of Governors of the Federal Reserve System v. MCorp Financial, Inc., 502 U.S. 32, 112 S.Ct. 459, 116 L.Ed.2d 358 (1991). In that case, the debtor contended that an investigation being conducted by the Federal Reserve was beyond its regulatory powers, and thus was not an exercise of governmental powers that could be excepted from the *366 Code's automatic stay provisions. The Court rejected that argument:

> MCorp contends that in order for § 362(b)(4) to obtain, a court must first determine whether the proposed exercise of police or regulatory power is legitimate and that, therefore, in this litigation the lower courts did have the authority to examine the legitimacy of the Board's actions and to enjoin those actions. We disagree. MCorp's broad reading of the stay provisions would require bankruptcy courts to scrutinize the validity of every administrative or enforcement action brought against a bankrupt entity. Such a reading is problematic, both because it conflicts with the broad discretion Congress has expressly granted many administrative entities and because it is inconsistent with the limited authority Congress has vested in bankruptcy courts. We therefore reject MCorp's reading of § 362(b)(4).

Id. at 40, 112 S.Ct. at 464. [FN5]

FN5. The Federal Reserve proceeding challenged by MCorp had not yet progressed beyond the Federal Reserve's expression of its intent to determine whether MCorp had violated banking regulations. In discussing whether these proceedings were automatically stayed pursuant to § 362(a)(3), the Court distinguished these investigations from proceedings that "culminate[d] in a final order" and further proceedings to enforce such an order. The latter, the Court suggested, might justify the exercise of jurisdiction by the bankruptcy court to enjoin enforcement of the final order. "We are not persuaded, however, that the automatic stay provisions of the Bankruptcy Code have any application to ongoing, nonfinal administrative proceedings." 502 U.S. at 41, 112 S.Ct. at 464. In the context of a discussion of § 362(a)(3), this sentence is merely a recognition that nonfinal proceedings are not "exercise[s] of control over [ ] property of the estate" that are stayed under that subsection. We do not read it to limit the Court's discussion of § 362(b)(4) to those cases involving "ongoing, nonfinal administrative proceedings."

[7][8][9] This is not to say that bankruptcy courts are without power to prevent a governmental unit's bad-faith exercise of its police or regulatory power against the estate. By creating exceptions for police and regulatory actions, "Congress removed local regulation only from the effect of the automatic stay; it did not eliminate the bankruptcy court's power to enjoin the enforcement of local regulation which is shown to be used in bad faith." In re National Hospital and Institutional Builders Co., 658 F.2d 39, 43 (2d Cir.1981). [FN6] However, the good faith of state and local officials "should be presumed, only to be rebutted by particularized pleadings made after investigation as required by Rule 9011 of the Rules of Bankruptcy Procedure and proof of the various forms of bad faith set forth in National Hospital." [FN7] In re Beker Industries Corp., 57 B.R. 611, 627 (Bankr.S.D.N.Y.1986). Javens did, in fact, seek an injunction from the bankruptcy court to prevent Hazel Park from proceeding with the demolition of the Blue Dot Building. Although Javens submitted an affidavit from a contractor, William Wallace, alleging discriminatory and oppressive treatment of Javens by Hazel Park, we do not find the required particularized pleadings of bad faith in Javens's Motion for Damages and Injunctive Relief, J.A. at 158, or his supplemental

filing, *367 J.A. at 186. There is no indication in the record that the bankruptcy court ever ruled on Javens's motion for an injunction and damages. Javens's appeals are limited, by their terms, to the bankruptcy court's orders exempting the cities from the automatic stay. Even if we were to treat the bankruptcy court's orders as denials of Javens's motion for an injunction, and this appeal as an appeal of that denial, the demolition of the buildings would render the case moot.

FN6. In re National Hospital was brought under the old Bankruptcy Act, under which there were no built-in exceptions for exercises of police or regulatory power. The court held that automatic stays under the Act were subject to challenges on grounds of bad faith.
The court in In re Beker Industries Corp., 57 B.R. 611, 627 (Bankr.S.D.N.Y.1986), extended this principle from injunctions to automatic stays: "Section § 362(b)(4), in its qualification 'to enforce such governmental unit's police or regulatory power,' apparently excludes actions or proceedings brought for an ulterior motive and thus in bad faith. We see no reason, moreover, why Congress would exempt bad faith regulation from the automatic stay and thereby make a debtor's preliminary freedom from it subject to a showing of injury.... Indeed, the district court for this district has effectively adopted that approach by engrafting the National Hospital reasoning on to the § 362(b)(4) exemption. See In re Lawson Burich Associates, 31 B.R. [604] at 610 (S.D.N.Y.1983); accord In re Farmers and Ranchers Livestock Auction, Inc., 46 B.R. 781 (Bankr.E.D.Ark.1984)." This holding, however, pre-dates and is effectively overruled by MCorp.

FN7. In In re National Hospital, the court held that a bankruptcy trustee seeking to bar governmental enforcement of a regulation has to show that the law or regulation is " 'flagrantly and patently violative of express constitutional prohibitions in every clause, sentence or paragraph, and in whatever manner and against whomever an effort might be made to apply it'; that the state forum is biased; that the City acted in wilful disregard of the law; that City officials clearly abused their discretion in initiating proceedings against the trustee; or that the 'state proceeding (was) motivated by a desire to harass.' " 658 F.2d at 44 (citations omitted).

Javens is not without recourse if the state and local authorities violated his rights. He has filed a lawsuit in Michigan state court alleging due process violations. A federal suit under 42 U.S.C. § 1983 might be another means of vindicating his rights.

B

[10] Javens also argues that the cities were not really exercising their police or regulatory power; instead, he contends, the enforcement of their building and fire codes fell under the rubric of "controlling the property of the estate." This characterization of the actions would confer one of two benefits on Javens. It could mean that an automatic stay was created under § 362(a)(3), which stays "any act to obtain possession ... or to exercise control over property of the estate," and for which no exception is available. Alternatively, if the automatic stay were viewed as being created under § 362(a)(1) or (2), the demolition orders, as actions definitionally distinct from exercises of police or regulatory power, would not be excepted from the stay by § 362(b)(4) or (5).

These arguments, in their extreme form, depend on the view that no logical intersection exists between the category of an "act ... to exercise control over property of the estate" and the category of an "action or proceeding ... to enforce [a] governmental unit's police or regulatory power." This, of course, is a false dichotomy. Many actions against a debtor taken under governmental police or regulatory power have the effect of controlling the property of the estate. Cf. MCorp, 502 U.S. at 41, 112 S.Ct. at 464 ("It is possible, of course, that the Board proceedings, like many other enforcement actions, may conclude with the entry of an order that will affect the Bankruptcy Court's control over the property of the estate, but that possibility cannot be sufficient to justify the operation of the stay against an enforcement proceeding that is expressly exempted by § 362(b)(4). To adopt such a characterization of enforcement proceedings would be to render subsection (b)(4)'s exception almost meaningless.").

A number of cases have explored how governmental actions falling within this overlapping territory should be treated for purposes of § 362 stays. In support of the proposition that the demolition orders were acts to control the property of the estate, Javens relies in part on In re Missouri, 647 F.2d 768 (8th Cir.1981). In that case, Missouri sought a writ of mandamus against the United States

Bankruptcy Court for the Eastern District of Arkansas, seeking recognition that proceedings the state had initiated against a debtor to enforce its grain regulatory laws were not subject to an automatic stay. At issue was whether the state could liquidate an insolvent grain warehouse (and presumably distribute the grain to the restive farmers who had deposited their harvest there), or whether the grain had to remain under control of the bankruptcy court. Missouri argued that enforcement of its grain regulations qualified for a § 362(b)(4) exception. The Eighth Circuit disagreed.

> [W]e believe that the term 'police or regulatory power' refers to the enforcement of state laws affecting health, welfare, morals, and safety, but not regulatory laws that directly conflict with the control of the res or property by the bankruptcy court.

Id. at 776. Javens invites the conclusion that demolition of their buildings "directly conflicts" with the bankruptcy court's control of the estate's property, and that under In re Missouri, there is no exception to the automatic stay.

Javens, however, does not cite the accompanying passage in the Eighth Circuit decision:

> We conclude that Missouri's grain laws, although regulatory in nature, primarily relate to the protection of the pecuniary interest in the debtors' property and not to matters of public safety and health. Missouri's laws, by governing the operation and liquidation of grain warehouses, directly conflict with the control of the property by the bankruptcy court and, therefore, do *368 not fall within the section § 362(b)(4) exception.

Id. at 776. This "pecuniary interest" distinction badly undercuts Javens's argument. [FN8] Although Javens argues in his brief that the Hazel Park action was "pecuniary" because the cost of demolition was to be assessed against the estate, we think that enforcing the city building codes did not relate in a meaningful way to any pecuniary interest of the cities. Further, as the bankruptcy court noted, Hazel Park was not a creditor of the estate. But the absence of pecuniary interest does not fully address the issue of whether the cities' actions "directly conflict[ed] with the control of the property by the bankruptcy court" in such a way as to render the (b)(4) and (5) exceptions inapplicable under In re Missouri.

FN8. In deciding whether particular government actions are excepted from the automatic stay, courts have also applied a "public policy test." See NLRB v. Edward Cooper Painting, Inc., 804 F.2d 934, 942 (6th Cir.1986). That analysis " 'distinguishes between proceedings that effectuate public policy and those that adjudicate private rights: only the former are excepted from the automatic stay.' " Ibid., quoting In re Herr, 28 B.R. 465, 468-69 (Bankr.D.Me.1983). Clearly, enforcement of building codes is an effectuation of public policy, rather than an adjudication of private rights.

It is first important to observe that when In re Missouri was issued, § 362(a)(3) covered only "any act to obtain possession of property of or from the estate." Congress amended that language in 1984 by adding the phrase "or to exercise control over property of the estate." Thus, it cannot be assumed that "control of the property" as discussed in In re Missouri is the same sort of "control" as is mentioned in the amendment to § 362(a)(3).

When Congress added the new language, it did so without explanation. And "the term 'control' is not defined in the 1984 amendments, nor is it generally defined in the Bankruptcy Code." See In re National Cattle Congress, Inc., 179 B.R. 588, 595 (Bankr.N.D.Iowa 1995), remanded on other grounds, 91 F.3d 1113 (8th Cir.1996); Beker Industries, 57 B.R. at 625. [FN9] The fact that "to obtain possession" was amended to "to obtain possession ... or to exercise control" hints, however, that this kind of "control" might be a broadening of the concept of possession, and thus similar in kind; e.g. "controlling" a corporation or its assets through voting trusts or shareholder agreements, rather than by "possessing" it outright. Id. at 626 ("Since an act designed to change control of property could be tantamount to obtaining possession and have the same effect, it appears that § 362(a)(3) was merely tightened to obtain full protection."). It could also have been intended to make clear that (a)(3) applied to property of the estate that was not in the possession of the debtor.

FN9. A nearly contemporaneous law review article about the amendments noted the "exercise control" provision without explanation other than to suggest it followed a pattern of greater explicitness in the automatic stay provisions. Ronald M. Martin and Terrence P. Fagan, A Guide to the Bankruptcy Amendments and Federal Judgeship Act of 1984, 13 Colo. Law. 1775, 1786 (1984). See also

Dennis Montali, Important Bankruptcy Code Changes in the Bankruptcy Amendments and Federal Judgeship Act of 1984, 332 PLI/Comm 61, 73 (1984) (noting new language without explanation).

Beker Industries was one of the first cases to address the meaning of "control" in the amended § 362(a)(3), and remains one of the most thoughtful explorations of the matter. Beker, the debtor, sought to enjoin-- through the automatic stays of § 362(a)(1) and/or (a)(3)--continuation by the Florida Land and Water Adjudicatory Commission of administrative proceedings to restrict Beker's shipping of phosphate rock from its mine to its refinery. For Florida to reduce the amount of rock it permitted Beker to ship on its highways, Beker argued, would be to control its property, since neither the mine nor the refinery could operate at desirable capacities if the transportation of rock from one to the other were restricted.

The bankruptcy court reasoned that such a reading of the word "control" made sense only if Congress intended the term to include state and local regulation of property (not just state and local efforts to establish or protect a pecuniary interest in property, as in In re Missouri). To have so legislated would have overruled the numerous cases excepting governmental regulation from automatic stays, which Congress would not likely have done without some strong expression of intent, especially in view of its clear intent--seen just six years earlier with the enactment of the Code--to create such an exception. Beker Industries, 57 B.R. at 626. ***369** The court "thus [held] that the scope of the control provision of § 362(a)(3), as applicable to governmental regulation, is governed by the contours of § 362(b)(4) as developed by case authority." Ibid. In other words, the universe of actions that trigger an automatic stay under § 362(a)(3) does not include those governmental actions entitled, under § 362(b)(4), to an exception from an automatic stay.

The district court relied in part on Cournoyer v. Town of Lincoln, 790 F.2d 971 (1st Cir.1986), aff'g 53 B.R. 478 (D.R.I.1985), a case in accord with Beker Industries. In Cournoyer, the defendant town had obtained, pursuant to its zoning ordinances, state court orders allowing it to remove and sell used truck parts in Cournoyer's salvage yard. [FN10] Cournoyer, the debtor, sought to enforce an automatic stay to prevent the town from proceeding. The district court decision in the case discussed in detail whether a § 362(a)(3) stay arose in the case, and in an analysis citing Missouri but presaging Beker, concluded that the removal and disposal of the truck parts were not acts to obtain possession or control of the debtor's property. "[S]uch a characterization is inappropriate, and has been rejected, because of the justification underlying the governmental action.... [T]he sole motivation for the official action ... is to stop the debtor from operating a business in violation of state or local law. [The government has] no pecuniary interest in the debtor's property, nor does the law under which it proceeds attempt to protect any other party's pecuniary interest." 53 B.R. at 483. Without identifying the particular subsection of § 362(a) from which an automatic stay arose, the First Circuit held that the § 362(b)(4) and (5) exceptions applied.

FN10. The proceeds of the sale were to be returned to Cournoyer, less the expenses of removal and sale. 53 B.R. at 485.

In opposition to Cournoyer, Javens heavily relies on Hillis Motors, Inc. v. Hawaii Automobile Dealers' Ass'n, 997 F.2d 581 (9th Cir.1993). [FN11] In that case, a Hawaii government agency (the "DCCA") dissolved Hillis Motors, a Hawaii corporation, for failing to file annual exhibits and pay filing fees as required by Hawaii law. At the time of the dissolution, Hillis Motors was a Chapter 11 debtor, and argued that the DCCA's action should have been automatically stayed. The district court held that § 362(a)(3) did not apply, because the DCCA's action concerned not Hillis Motors's property, but its status. The Ninth Circuit reversed, stating:

FN11. Hazel Park and Royal Oak argue that Hillis Motors is distinguishable in that the statute under which DCCA dissolved Hillis Motors did not affect health, welfare, and safety in the way building codes do.

There is no question that the DCCA exercised control over Hillis' corporate property by involuntarily dissolving Hillis. When a corporation is involuntarily dissolved by the DCCA, that action serves to vest legal and equitable title to all corporate property in the stockholders.... Thus, the effect of Hillis'

dissolution was to transfer all corporate property to the stockholders. Since all corporate property also passes to the estate when a bankruptcy petition is filed ... there is also no doubt that ... the DCCA exercised control over property that belonged to the estate just following the commencement of Hillis' bankruptcy case.

Id. at 586-87. The court held that the DCCA's action was stayed by § 362(a)(3), for which there was no exception. Hence the dissolution was void ab initio, and Hillis Motors remained a corporation with standing to sue the defendant.

Hillis Motors does not discuss Beker Industries, but rejects the holding of that case that actions by governmental units to enforce their police or regulatory power are excepted from automatic stays otherwise arising under § 362(a)(3). The Ninth Circuit held that even if the structure of § 362 did not make it clear that the (b)(4) and (b)(5) exceptions did not apply to an (a)(3) stay,

we would still hold that the governmental powers exceptions do not apply here. We agree with the Eighth Circuit [in In re Missouri] that the terms 'police or regulatory power' as used in those exceptions refer to the enforcement of state laws affecting health, morals, and safety but not regulatory laws that directly conflict with *370 the control of the res or property by the bankruptcy court.

997 F.2d at 591.

But this analysis is fraught with difficulty. Like the original formulation in In re Missouri, it fails to account for actions that are undoubtedly exercises of police or regulatory power and that also, in some way, conflict with the control of the property of the estate by the bankruptcy court. Worse, Hillis Motors discounts the "pecuniary interest" distinction with which the Eighth Circuit partly solved that difficulty. [FN12] Finally, the case fails to consider the possible difference between the Eighth Circuit's usage of "control," and Congress's later usage of the same word § 362(a)(3). Beker Industries, by contrast, convincingly explains why the In re Missouri "control" analysis should not apply to the amended § 362(a)(3).

FN12. "While [the 'pecuniary interest' theory] seems an unduly narrow interpretation of the Eighth Circuit's decision, assuming this were a valid distinction, it is not availing to the appellees." Hillis Motors, 997 F.2d at 591 n. 19.

V

[11][12] In support of his argument that automatic stays arose under (a)(3), Javens also argues that (a)(1) can't apply because that subsection speaks of actions against the debtor, and the demolition orders were, by contrast, in rem. [FN13] It is true that (a)(1) refers only to actions against the debtor, whereas other subsections of § 362(a) refer to actions against property. And it is true that some in rem actions, such as acts to create, perfect, or enforce liens against property of the estate, see § 362(a)(4), or of the debtor, see § 362(a)(5), are automatically stayed without exception. But it is beyond doubt that the Code cannot have the meaning that Javens suggests. Numerous governmental aims falling plainly within the police and regulatory power are enforced by means of actions in rem. See, e.g., 7 U.S.C. § 136k(b) (authorizing in rem proceedings to seize adulterated or mislabeled pesticides); 15 U.S.C. § 1195(b) (same, with respect to goods in violation of Flammable Fabrics Act); 15 U.S.C. § 2626 (same, with respect to compounds in violation of Toxic Substances Control Act); M.C.L.A. 289.711 (authorizing detention, embargo, and condemnation of adulterated or mislabeled food). If none of these were excepted from the automatic stays, the purpose of § 362(b)(4) would be grossly compromised. Clearly, § 362(a)(1) is not limited to in personam actions.

FN13. The lawsuit by Hazel Park was styled as being against the Javenses and other individuals. Judge Nichols's demolition order of February 2, 1994, was similarly captioned. On the other hand, Hazel Park Building Code § 15.04.190 separately describes actions against persons for violations (punishable by fine or imprisonment) and actions against buildings, which if declared to be a nuisance, may be ordered abated. See also Hazel Park Property Maintenance Code § 15.09.060. Thus, despite its caption, the first Hazel Park demolition order was seemingly an action in rem. The Royal Oak demolition order is styled "IN RE: Premises Located at 213 Euclid," and the order is clearly issued against the house.

The Royal Oak and first Hazel Park demolition orders, and the continuing Hazel Park litigation over 422 East George Street, all fit well within the language of § 362(a)(1). That provision is then

subject to the exception provision of § 362(b)(4). As we concluded above, the cities' actions were exercises of their police power within the meaning of (b)(4). Therefore, the cities' actions enjoyed an exception to the stay, which the bankruptcy court and district court correctly recognized.

VI

[13] We acknowledge that there is authority for reaching a different conclusion in a case, such as this one, where the exercise of police or regulatory power has the effect of destroying property of the estate. In In re National Cattle Congress, Inc., 179 B.R. 588, 597-98 (Bankr.N.D.Iowa 1995), remanded on other grounds, 91 F.3d 1113 (8th Cir.1996), for example, where the state agency sought to revoke the debtor's racing license, the bankruptcy court held that the agency would first have to seek relief from the automatic stay because "[r]evocation constitutes maximum control over Debtor's racing license as the act destroys any value which this property has to the estate." [FN14] Javens has argued vigorously for this proposition. We conclude that the (b)(4) and (b)(5) exceptions are not intended to be limited to non- *371 destructive exercises of governmental power. Many governmental actions clearly within the police or regulatory power destroy some or all of the value that property has to an estate. The limitation would too often void an exception Congress wrote into the law.

FN14. Cf. Beker Industries, in which the bankruptcy court, before holding that the state's trucking regulations were excepted from the automatic stay, observed that "[t]here is no indication that the Commission Proceeding currently poses a threat to Beker's property." 57 B.R. at 623 (S.D.N.Y.1986). The debtor had argued that a stay should apply where the regulatory action posed a threat to the property of the estate. The court noted that it found no authority to support that argument, and that, in any event, the state's action did not so threaten the debtor's property.

[14] Even if we subscribed to the view of In re National Cattle Congress, the cities would still have been mostly immune from damages for their actions. Section 362(h) allows "an individual injured by any willful violation of a stay provided by this section [to] recover actual damages, including costs and attorneys' fees, and, in appropriate circumstances, [to] recover punitive damages." Hazel Park and Royal Oak obtained orders from the bankruptcy court declaring that there was no stay in force to prevent the enforcement of their building and fire codes. Even if the bankruptcy court were wrong, and the cities should not have enjoyed exceptions to the automatic stays, it could scarcely be said that the cities willfully violated stays that court orders declared did not exist. [FN15]

FN15. Javens alleges that Hazel Park directed local utility companies to cut service to the Blue Dot Building, causing frozen pipes and related damage, prior to the bankruptcy court's order recognizing that the automatic stay did not apply. This order would not have shielded the cities from liability for these damages.

VII

The judgment of the district court is AFFIRMED.

END OF DOCUMENT

132 F.3d 591
31 Bankr.Ct.Dec. 1163, Bankr. L. Rep. P 77,592, 97 CJ C.A.R. 3440, 15 Colo. Bankr. Ct. Rep. 29
(Cite as: 132 F.3d 591)

In re: YELLOW CAB COOPERATIVE ASSOCIATION, Debtor.
YELLOW CAB COOPERATIVE ASSOCIATION,
Plaintiff-Appellant,
v.
METRO TAXI, INC., a Colorado Corporation; Colorado Transportation, Inc., a Colorado Corporation dba American Cab Company,
Defendants,
and
Bruce Smith, in his official capacity of Executive Director of the Public Utilities Commission; Leland Smith, in his official capacity; Philip Smith, in his official capacity; Ronald Jack, in his official capacity; Gray Gramlick, in his official capacity; Gordon King, in his official capacity; West Twomey, in his official capacity; Bob Laws, in his official capacity; Colorado Public Utilities Commission, an agency of the State of Colorado; Robert J. Hix, in his capacity as Commissioner; Vincent Majkowski, in his capacity as Commissioner; Christine E.M. Alvarez, in her capacity as Commissioner, Defendants-Appellees.

No. 96-1443.

United States Court of Appeals, Tenth Circuit.

Dec. 23, 1997.

In connection with sale of Chapter 11 debtor-taxicab company's sale of assets, debtor sought injunction prohibiting state public utilities commission and other cab companies from opposing full transfer of debtor's operating certificate, which authorized debtor to operate up to 600 cabs in designated city. Commission issued transfer decision limiting transfer of authority to 300 cabs. The Bankruptcy Court permanently enjoined commission from enforcing transfer decision. Commission appealed. After granting commission's motion for stay pending appeal, 192 B.R. 555, and denying debtor's motions to dismiss appeal or vacate stay, 194 B.R. 504, the United States District Court for the District of Colorado, John L. Kane, Jr., J., 200 B.R. 237, reversed and vacated injunction. Debtor appealed. The Court of Appeals, Anderson, Circuit Judge, held that: (1) commission's decision not to approve full transfer of debtor's operating certificate was governmental regulatory action excepted from automatic stay, and (2) governmental regulatory or police power exception to automatic stay concerning commencement or continuation of action or proceeding to enforce police or regulatory power applies to actions stayed under automatic stay provision barring acts to obtain possession of or control over estate property.

District court affirmed.

[1] FEDERAL COURTS ⇐12.1
170Bk12.1
Article III mootness is doctrine of standing set in time frame: requisite personal interest that must exist at commencement of litigation (standing) must continue throughout its existence (mootness). U.S.C.A. Const.Art. 3, § 2, cl. 1.

[2] FEDERAL CIVIL PROCEDURE ⇐103.2
170Ak103.2
Both standing and mootness are threshold jurisdictional issues.

[2] FEDERAL COURTS ⇐12.1
170Bk12.1
Both standing and mootness are threshold jurisdictional issues.

[3] FEDERAL CIVIL PROCEDURE ⇐103.2
170Ak103.2
To have standing, plaintiff must have suffered actual injury; that is, invasion of legally protected interest which is (a) concrete and particularized, and (b) actual or imminent, not conjectural or hypothetical.

[4] FEDERAL CIVIL PROCEDURE ⇐103.3
170Ak103.3
To have standing, plaintiff must show that it is likely that injury will be redressed by favorable decision.

[5] FEDERAL CIVIL PROCEDURE ⇐103.2
170Ak103.2
Standing must be demonstrated throughout appeal; plaintiff must maintain standing at all times throughout litigation for court to retain jurisdiction.

[5] FEDERAL COURTS ⇐545.1
170Bk545.1

Standing must be demonstrated throughout appeal; plaintiff must maintain standing at all times throughout litigation for court to retain jurisdiction.

[6] FEDERAL COURTS ⚿12.1
170Bk12.1
Case is "moot" when issues presented are no longer live or parties lack legally cognizable interest in outcome.
See publication Words and Phrases for other judicial constructions and definitions.

[7] BANKRUPTCY ⚿3781
51k3781
Court of Appeals would consider merits of appeal from district court's vacation of injunction issued by bankruptcy court against state public utilities commission, which barred commission from enforcing its decision that precluded full transfer of Chapter 11 debtor-taxicab company's operating certificate to purchaser of debtor's assets, given possibility that debtor continued to face liability to purchaser's assignee as result of impaired certificate, despite settlement agreement between them, and thus that controversy was not yet moot.

[8] BANKRUPTCY ⚿3782
51k3782
Court of Appeals' review of district court's factual and legal determinations is governed by same standards district court used to review bankruptcy court; thus, it reviews de novo legal decisions of bankruptcy and district courts, and reviews bankruptcy court's factual findings for clear error.

[8] BANKRUPTCY ⚿3786
51k3786
Court of Appeals' review of district court's factual and legal determinations is governed by same standards district court used to review bankruptcy court; thus, it reviews de novo legal decisions of bankruptcy and district courts, and reviews bankruptcy court's factual findings for clear error.

[9] BANKRUPTCY ⚿2402(4)
51k2402(4)
State public utilities commission's decision not to approve full transfer of Chapter 11 debtor-taxicab company's operating certificate to purchaser of debtor's assets, reducing operation authority from 600 to 300 cabs, was "governmental regulatory action" and thus was excepted from automatic stay provision precluding commencement or continuation of action or proceeding against debtor; reduction resulted from debtor's nonuse of full operating authority and potential for damages to other carriers and public interest arising from any reactivation of debtor's dormant rights. Bankr.Code, 11 U.S.C.A. § 362(a)(1), (b)(4).
See publication Words and Phrases for other judicial constructions and definitions.

[10] BANKRUPTCY ⚿2402(4)
51k2402(4)
Even if stay provision applicable to state public utilities commission's action in refusing to approve full transfer of Chapter 11 debtor-taxicab company's operating certificate to purchaser of debtor's assets was provision barring acts to obtain possession of or control over estate property, commission's action was excepted from automatic stay under governmental regulatory or police power exception. Bankr.Code, 11 U.S.C.A. § 362(a)(3), (b)(4).

[11] BANKRUPTCY ⚿2402(1)
51k2402(1)
Governmental regulatory or police power exception to automatic stay concerning commencement or continuation of action or proceeding to enforce police or regulatory power applies to actions stayed under automatic stay provision barring acts to obtain possession of or control over estate property. Bankr.Code, 11 U.S.C.A. § 362(a)(3), (b)(4).
*593 E. Hil Margolin, Denver, CO, for appellant.

Neil L. Tillquist, Assistant Attorney General (Gale A. Norton, Attorney General, with him on the brief), Denver, CO, for appellees.

Before ANDERSON, KELLY and HENRY, Circuit Judges.

ANDERSON, Circuit Judge.

Yellow Cab Cooperative Association, Inc. appeals from a district court decision overturning an injunction entered against the Colorado Public Utilities Commission ("PUC") by the bankruptcy court. The district court held that the bankruptcy court improperly enjoined the PUC from restricting the scope of a certificate it had issued to Yellow Cab. We affirm the district court's order overturning the injunction issued by the bankruptcy court, and hold that the PUC's action was a valid

exercise of its regulatory power and, as such, was exempt under 11 U.S.C. § 362(b)(4) and (5) from the automatic stay provisions of the Bankruptcy Code.

BACKGROUND

Yellow Cab filed a voluntary petition under Chapter 11 of the Bankruptcy Code on December 31, 1993. It thereafter negotiated a sale of its assets to Taxi Associates, Inc., outside the ordinary course of business pursuant to 11 U.S.C. § 363(b), (f), and (m), which the bankruptcy court authorized. Among Yellow Cab's assets was Certificate of Public Convenience and Necessity No. 2378 & I ("CPCN No. 2378 & I"), issued by the PUC, which authorized Yellow Cab to operate up to 600 cabs in the Denver metropolitan area. Over the preceding five years, however, Yellow Cab had in fact operated approximately 300 cabs under CPCN No. 2378 & I.

Because the sale of assets involved the sale of PUC operating certificates, the bankruptcy court directed Yellow Cab and Taxi Associates to apply to the PUC for approval of the transfer of the certificates. Yellow Cab and an assignee of Taxi Associates filed a joint application before the PUC seeking authorization to transfer Yellow Cab's operating authority, including CPCN No. 2378 & I, to Taxi Associates. Two other cab companies, Metro Cab and American Cab, as well as the PUC Staff, filed written objections to the transfer application, arguing that part of Yellow Cab's authority to operate up to 600 cabs under CPCN No. 2378 & I had become dormant through non-use.

An administrative law judge held hearings on the application, and subsequently issued an advisory opinion recommending that the PUC approve the transfer of the full operating authority--up to 600 cabs--authorized by CPCN No. 2378 & I. The PUC disagreed with the administrative law judge. It issued its decision ("Transfer Decision") on Yellow Cab's transfer petition, overturning the ALJ's recommendation and refusing to allow the transfer of authority under CPCN No. 2378 & I in excess of 300 cabs. The PUC held that the unused authority under the CPCN had become dormant and transfer of the full authority would cause destructive competition which would be against the public interest.

While proceedings were pending before the PUC, Yellow Cab initiated this adversary *594 proceeding in the bankruptcy court against the PUC, Metro Cab, and American Cab, seeking an injunction prohibiting them from opposing the transfer of the full 600 cab authority under CPCN No. 2378 & I. The bankruptcy court ultimately issued an order permanently enjoining the PUC from enforcing the Transfer Decision on the ground that the Transfer Decision limiting CPCN No. 2378 & I to 300 cabs had the effect of "controlling" property of the estate in violation of 11 U.S.C. § 362(a)(3), one of the Bankruptcy Code's automatic stay provisions.

The PUC filed a notice of appeal from the bankruptcy court's order, as well as a motion for stay pending appeal. The bankruptcy court denied the motion, and ordered the PUC "forthwith to authorize [Yellow Cab] to transfer its total operating authority under the [Certificate] of 600 vehicles to Taxi Associates." Colorado Pub. Utils. Comm'n v. Yellow Cab Co-op. Ass'n (In re Yellow Cab), 194 B.R. 504, 506 (D.Colo.1996). The PUC issued the Certificate, with the caveat that it was "subject [to] future modifications by the United States Federal Courts that may result from any appeal by the Public Utilities Commission of" the bankruptcy court's order. Id. at 507.

The following day, February 9, 1996, Yellow Cab and Taxi Associates closed the sale of assets. One week later, the PUC filed a motion in the district court for a stay pending appeal, which the district court granted. Colorado Pub. Utils. Comm'n v. Yellow Cab Co-op. Ass'n (In re Yellow Cab), 192 B.R. 555 (D.Colo.1996). Yellow Cab then filed a motion to dismiss the PUC's appeal as moot or, alternatively, to vacate the stay. In reliance on the stay, the PUC reissued CPCN No. 2378 & I, with a limit of 300 cabs. The district court denied Yellow Cab's motions. In re Yellow Cab, 194 B.R. at 508. In its third order, the one from which Yellow Cab appeals in this case, the district court overturned the bankruptcy court's injunction, holding that two exceptions to the automatic stay provisions, 11 U.S.C. § 362(b)(4) and (5), which exempt from the automatic stay certain governmental action designed to enforce the government's police or regulatory power, applied and permitted the PUC to reduce the authority transferred by the CPCN to 300 cabs. Colorado Pub. Utils. Comm'n v. Yellow Cab Co-

op. Ass'n (In re Yellow Cab), 200 B.R. 237 (D.Colo.1996). Yellow Cab appeals. The PUC has filed a motion to dismiss the appeal on the ground that Yellow Cab lacks standing and/or the case has become moot. Yellow Cab argues that we should vacate the district court decision, as the case had become moot prior to the issuance of that decision.

DISCUSSION

I. Standing and Mootness

[1][2][3][4][5][6][7] We first address the PUC's argument that Yellow Cab lacks standing and the case has become moot. "Article III mootness is 'the doctrine of standing set in a time frame: The requisite personal interest that must exist at the commencement of the litigation (standing) must continue throughout its existence (mootness).' " Southern Utah Wilderness Alliance v. Smith, 110 F.3d 724, 727 (10th Cir.1997) (quoting Arizonans For Official English v. Arizona, --- U.S. ----, ----, 117 S.Ct. 1055, 1069, 137 L.Ed.2d 170 (1997)). Both standing and mootness are threshold jurisdictional issues. Keyes v. School Dist. No. 1, 119 F.3d 1437, 1445 (10th Cir.1997); McClendon v. City of Albuquerque, 100 F.3d 863, 867 (10th Cir.1996). To have standing, a plaintiff must have suffered an actual injury--" 'an invasion of a legally protected interest which is (a) concrete and particularized, and (b) actual or imminent, not conjectural or hypothetical.' " Keyes, 119 F.3d at 1445 (quoting Lujan v. Defenders of Wildlife, 504 U.S. 555, 560, 112 S.Ct. 2130, 2136, 119 L.Ed.2d 351 (1992)). Moreover, to have standing a plaintiff must show that " 'it is likely that the injury will be redressed by a favorable decision.' " Roe v. Cheyenne Mountain Conference Resort, Inc., 124 F.3d 1221, 1229 (10th Cir.1997) (quoting United States v. Colorado Supreme Ct., 87 F.3d 1161, 1164 (10th Cir.1996)). Finally, standing must be demonstrated throughout an appeal: "a plaintiff must maintain standing at all times throughout the litigation for a court to retain jurisdiction." Powder River Basin Resource Council v. Babbitt, 54 F.3d 1477, 1485 (10th Cir.1995). Similarly, " 'a case is *595 moot when the issues presented are no longer "live" or the parties lack a legally cognizable interest in the outcome.' " County of Los Angeles v. Davis, 440 U.S. 625, 631, 99 S.Ct. 1379, 1383, 59 L.Ed.2d 642 (1979) (quoting Powell v. McCormack, 395 U.S. 486, 496, 89 S.Ct. 1944, 1951, 23 L.Ed.2d 491 (1969)); see also City of Albuquerque v. Browner, 97 F.3d 415, 420 (10th Cir.1996), cert. denied, --- U.S. ----, ----, 118 S.Ct. 410, ----, 139 L.Ed.2d 314 (1997).

In this case, Yellow Cab now arguably lacks any legally cognizable interest in the outcome. Yellow Cab closed on the sale of its assets to Taxi Associates on February 9, 1996. The sale agreement specifically provided that no representations and warranties concerning the transferred assets, including CPCN 2378 & I, survived the closing. No one disputes that Taxi Associates was aware of the controversy concerning the scope of the authority granted by CPCN 2378 & I, but nonetheless purchased Yellow Cab's assets without reserving the right to complain later about the scope of that authority. However, as long as the possibility remained that Taxi Associates could collaterally attack, or attempt to "undo," the sale because the scope of the authority was subsequently reduced to 300 cabs, Yellow Cab remained at risk for some additional liability. Indeed, Taxi Associates' assignee, Denver Taxi, took just such action: it filed an application for an administrative expense priority claim against Yellow Cab's estate in the amount of $437,311 for damages allegedly suffered by Denver Taxi due to the PUC's reduction of the CPCN's operating authority from 600 to 300 cabs.

Subsequently, however, Denver Taxi and Yellow Cab entered into a settlement agreement, which has been submitted for approval to the bankruptcy court. [FN1] Pursuant to the settlement agreement, Yellow Cab has agreed to continue to prosecute this case, and Denver Taxi completely releases Yellow Cab from any liability in connection with the sale of assets and proceedings before the PUC. Thus, Denver Taxi has released any claim it could have against Yellow Cab based on the scope of the authority transferred under CPCN 2378 & I. If the settlement agreement is approved, Yellow Cab will suffer no "injury," economic or otherwise, no matter what the outcome of this appeal. In that event, the controversy will indeed be moot, as far as Yellow Cab is concerned. [FN2]

FN1. At oral argument of this case, we granted the PUC's motion to supplement the record with a copy of the settlement agreement.

FN2. Yellow Cab argues that, because the sale of

> its assets to Taxi Associates occurred prior to the district court's decision, the case has actually been moot since the date of the closing on the sale, and therefore the district court lacked jurisdiction to overturn the bankruptcy court's injunction. We disagree. If the case has become moot, it is because Yellow Cab has, subsequent to the sale, negotiated an agreement pursuant to which it will suffer no injury whether or not the district court's decision is upheld. The closing of the asset purchase agreement did not by itself destroy Yellow Cab's standing. The possibility remained that Taxi Associates might seek to hold Yellow Cab liable for the diminished cab authority transferred under CPCN 2378 & I. And that is precisely what Taxi Associates' assignee did. It is because Yellow Cab has settled that claim, assuming the settlement agreement stands, and is no longer at risk for any judgment based on such a claim, that Yellow Cab's standing has evaporated, and the case between Yellow Cab and the PUC is moot.

However, the record reveals that the settlement agreement, as of now, has not been approved by the bankruptcy court, and the parties have not notified us to the contrary. Even if approved, such approval would presumably be subject to challenge on appeal. We therefore cannot say with certainty that the case is moot. We accordingly alternatively consider the merits of Yellow Cab's appeal.

II. Exemption to Automatic Stay

11 U.S.C. § 362(a) provides in pertinent part:

> Except as provided in subsection (b) of this section, a petition filed under section 301, 302, or 303 of this title ... operates as a stay, applicable to all entities, of -
> (1) the commencement or continuation ... of a judicial, administrative, or other action or proceeding against the debtor that was or could have been commenced before the commencement of the case under this title;
>
> *596 ....
>
> (3) any act to obtain possession of property of the estate or of property from the estate or to exercise control over property of the estate....

11 U.S.C. § 362(a)(1), (3). The bankruptcy court held that CPCN 2378 & I was property of the estate, and that the PUC's Transfer Decision, reducing the scope of its authority from 600 cabs to 300 cabs, had the effect of taking property from the estate in violation of § 362(a)(3). 11 U.S.C. § 362(b)(4) and (5) provide the following exceptions to the automatic stay:

> The filing of a petition under section 301, 302, or 303 of this section ... does not operate as a stay-
>
> ....
>
> (4) under subsection (a)(1) of this section, of the commencement or continuation of an action or proceeding by a governmental unit to enforce such governmental unit's police or regulatory power;
> (5) under subsection (a)(2) of this section, of the enforcement of a judgment, other than a money judgment, obtained in an action or proceeding by a governmental unit to enforce such governmental unit's police or regulatory power....

11 U.S.C. § 362(b)(4), (5). The bankruptcy court held that the "plain language" of § 362(b)(4) and (5) demonstrates that they only apply to actions under § 362(a)(1) and (2), not under § 362(a)(3). However, the court held that:

> since virtually all actions to which the automatic stay would apply can be characterized as actions "to obtain possession of property of the estate or of property from the estate, or to exercise control over the property of the estate ..." pursuant to 11 U.S.C. § 362(a)(3), the exceptions for police and regulatory actions contained in 11 U.S.C. § 362(b)(4) would be rendered meaningless if § 362(a)(3) were allowed to stay all actions by a regulatory agency which could affect the estate.

Yellow Cab Co-op. Ass'n v. Metro Taxi, Inc. (In re Yellow Cab), No. 93 23733 DEC, slip op. at 6, Appellant's App. at 47 [hereinafter "Order"]. The court therefore considered the PUC's Transfer Decision "as if [it] fell under § 362(a)(1) or (2)," but concluded that the exceptions contained in § 362(b)(4) and (5) did not apply. Id. Its only stated reasons for concluding that those exceptions did not apply were that § 362(b)(4) must be construed narrowly to permit governmental units to protect the public health and safety, as opposed to protecting a pecuniary interest in the debtor's property, and the PUC's action with respect to CPCN 2378 & I was "solely directed against the property of [Yellow Cab], which does not protect an important public interest." Id. at 7.

The district court disagreed with the bankruptcy court's narrow interpretation of § 362(b)(4), and held that, under Eddleman v. United States Dep't of

Labor, 923 F.2d 782, 785-86 (10th Cir.1991), the PUC's Transfer Decision was exempt from the automatic stay under § 362(b)(4) as governmental regulatory action designed to serve the public interest, not to advance the government's pecuniary interest in Yellow Cab's property. While not explicitly so stating, the district court implicitly agreed with the bankruptcy court's determination that the Transfer Decision fell under § 362(a)(1) of the automatic stay provision, not § 362(a)(3).

Yellow Cab argues the PUC's Transfer Decision is properly characterized as an action to "control" property of the estate under § 362(a)(3), and the plain language of the exemptions contained in § 362(b)(4) and (5) demonstrates that they do not apply to actions taken under § 362(a)(3). The PUC argues that its Transfer Decision is not subject to the automatic stay of § 362(a)(3), but, even if it were, the exceptions contained in § 362(b)(4) and (5) apply.

[8] "Our review of the district court's factual and legal determinations is governed by the same standards the district court used to review the bankruptcy court." Taylor v. Internal Revenue Serv., 69 F.3d 411, 415 (10th Cir.1995). Thus, we review de novo the legal decisions of the bankruptcy and district courts. Morrissey v. Internal Revenue Serv. (In re EWC, Inc.), 114 F.3d 1071, 1073 (10th *597 Cir.1997). We review the bankruptcy court's factual findings for clear error. Conoco, Inc. v. Styler (In re Peterson Distrib., Inc.), 82 F.3d 956, 959 (10th Cir.1996). "A finding of fact is clearly erroneous if it is without factual support in the record or if, after reviewing all of the evidence, we are left with the definite and firm conviction that a mistake has been made." Id.

This issue involves several subsidiary and interrelated inquiries--which automatic stay provision applies to bar the Transfer Decision and whether the exception for governmental regulatory authority contained in § 362(b)(4) or (5) applies to exempt the Decision from the automatic stay. Either § 362(a)(1) or (a)(3) applied to initially stay the Transfer Decision. If it was stayed under (a)(1), § 362(b)(4) lifted the stay, assuming the requirements of (b)(4) were met. If it was stayed under (a)(3), we must consider whether (b)(4) has any relevance to (a)(3) even though not explicitly referenced therein. In either event, we must consider whether the PUC's action was an exercise of governmental regulatory authority under § 362(b)(4) [FN3], so we turn first to that question.

> FN3. We focus primarily on § 362(b)(4), although we recognize that (b)(5) is arguably applicable as well. Section 362(b)(5) addresses "the enforcement of a judgment ... obtained in an action or proceeding by a governmental unit," while (b)(4) address the actual "action or proceeding." Thus, our discussion of (b)(4) will suffice to cover the substantive application of (b)(5) as well.

A. § 362(b)(4):

[9] In Eddleman v. United States Dep't of Labor, 923 F.2d 782 (10th Cir.1991) we discussed the parameters of § 362(b)(4) as follows:

> [C]ourts have developed two tests for determining whether agency actions fit within the [§ 362(b)(4)] exception. Under the "pecuniary purpose" test, the court asks whether the government's proceeding relates primarily to the protection of the government's pecuniary interest in the debtor's property and not to matters of public policy. If it is evident that a governmental action is primarily for the purpose of protecting a pecuniary interest, then the action should not be excepted from the stay. In contrast, the "public policy" test distinguishes between government proceedings aimed at effectuating public policy and those aimed at adjudicating private rights. Under this second test, actions taken for the purpose of advancing private rights are not excepted from the stay.

Id. at 791 (citations omitted); see also Wyoming Dep't of Transp. v. Straight (In re Straight), 209 B.R. 540, 544 (D.Wyo.1997). Under that test, the PUC's Transfer Decision would be subject to § 362(b)(4) if it effectuated public policy, as opposed to furthering the PUC's pecuniary interest in Yellow Cab's property.

The bankruptcy court held, with little explanation, that "the reduction in the number of cabs transferred represents an action solely directed against the property of [Yellow Cab], which does not protect an important public interest. It does not address the public welfare as does an action to stop violation of environmental protection laws; or an action to enforce bail in a criminal proceeding." Order at 7,

Appellant's App. at 48 (citations omitted). The district court held that that conclusion was reversible error and we agree.

As the district court observed, the PUC reduced the scope of the authority contained in CPCN 2378 & I because of Yellow Cab's non-use of its full operating authority "and [because of] damages to other carriers or to the public interest as a result of [any] reactivation of dormant rights." Transfer Decision at 17-18, Appellee's App. at 17-18. The PUC further stated, "the record is sufficient to show that destructive competition may result by unconditional approval of the transfer," id. at 20, and that "[t]he record also shows that approval of the transfer, with the right to use 600 vehicles, would likely damage other carriers and the public interest." Id. at 20-21. The bankruptcy court clearly erred in holding that the PUC's action was directed solely at Yellow Cab's property and not to effectuate public policy or public interest. Thus, the PUC's Transfer Decision is governmental regulatory action under § 362(b)(4), exempt from the automatic stay *598 of 362(a)(1). Because Yellow Cab argues that the stay provision applicable to the PUC's action was § 362(a)(3), not § 362(a)(1), we must next address whether § 362(a)(3) permits an exception for governmental regulatory authority under § 362(b)(4).

B. § 362(a)(3):

[10] 11 U.S.C. § 362(a)(3) stays acts "to obtain possession of property of the estate" or "to exercise control over property of the estate." The control language was added in 1984. As one court has observed, "[p]rior to this amendment, few, if any, cases exist in which administrative action was contested under § 362(a)(3) as compared to § 362(a)(1)." In re National Cattle Congress, Inc., 179 B.R. 588, 595 (Bankr.N.D.Iowa 1995), remanded on other grounds, 91 F.3d 1113 (8th Cir.1996). Because many governmental regulatory actions can be characterized as exercising control over a debtor's property, "the addition of the control language has sufficiently changed the focus of § 362(a)(3) to invite litigation in the area of administrative agency action under both sections." Id. Courts have struggled, in particular, to reconcile the fact that governmental police or regulatory power is clearly exempted from the stay imposed by (a)(1), but not clearly exempted from the stay imposed by (a)(3), despite the fact that comparable governmental administrative action might be involved. One way courts have accomplished that reconciliation is by construing the term "control" in (a)(3) with reference to § 362(b)(4).

An often-cited, and thoughtful, analysis of the term "control" in § 362(a)(3) appears in Beker Indus. Corp. v. Florida Land and Water Adjudicatory Comm'n (In re Beker Indus. Corp.), 57 B.R. 611, 626 (Bankr.S.D.N.Y.1986):

> In asserting coverage by § 362(a)(3) on a control theory, Beker contends that by regulating transport from the mine, the County and the Commission are exerting control over it. This argument has appeal only if by employing the term "control," Congress sought to include state and local regulation, as opposed to the limitation on the § 362(b)(4) exemption applicable to the automatic stay of acts against a debtor, such as state attempts to enforce state distribution schemes with respect to property of the estate ... or governmental acts to establish or protect a pecuniary interest in estate property.... To have done so through enacting the phrase and concomitantly failing to have amended § 362(b)(4) to exempt good faith exercise of police and regulatory power from § 362(a)(3) would have legislatively overruled the numerous cases exempting such governmental acts from the automatic stay....

Following Beker, a number of courts narrowly interpret § 362(a)(3), consistent with its legislative history, to apply "to prevent dismemberment of the estate" and to assure its orderly distribution. H.R.Rep. No. 595, 95th Cong., 1st Sess. 340, 341 (1977), reprinted in 1978 U.S.C.C.A.N. at 6298. Beker concluded that "the scope of the control provision of § 362(a)(3), as applicable to governmental regulation, is governed by the contours of § 362(b)(4) as developed by case authority." In re Beker Indus. Corp., 57 B.R. at 626.

[11] We agree with those courts which have held that the governmental regulatory or police power exception of § 362(b)(4) applies to actions stayed under § 362(a)(3). We recognize that there is some disagreement on this point, but conclude that the better reasoned view is that expressed in Beker. See Javens v. City of Hazel Park (In re Javens), 107

F.3d 359, 369 (6th Cir.1997) ("[T]he universe of actions that trigger an automatic stay under § 362(a)(3) does not include those governmental actions entitled, under § 362(b)(4), to an exception from an automatic stay."); Universal Life Church, Inc. v. United States (In re Universal Life Church, Inc.), 191 B.R. 433, 442 (E.D.Cal.1995) (rejecting the view that § 362(b)(4) applies only to stays under § 362(a)(1)), aff'd in part and appeal dismissed in part, 128 F.3d 1294 (9th Cir.1997); In re National Cattle Congress, Inc., 179 B.R. at 595 (agreeing with Beker); Official Comm. of Unsecured Creditors v. PSS Steamship Co. (In re Prudential Lines, Inc.), 107 B.R. 832, 843 (Bankr.S.D.N.Y.1989) (agreeing with Beker); *599 cf. Slater v. Town of Albion (In re Albion Disposal, Inc.), 203 B.R. 884, 887 (Bankr.W.D.N.Y.1996) ("[S]ome exercises of control by a governmental entity are so inextricably linked to (or otherwise are indistinguishable from) the type of (a)(1) action that (b)(4) forgives, that (a)(3) should be ignored entirely when the (b)(4) defense is found to exist."), aff'd in part and remanded in part, 1997 WL 461997 (W.D.N.Y. Aug.11, 1997). But see Hillis Motors, Inc. v. Hawaii Auto. Dealers' Ass'n, 997 F.2d 581, 591 (9th Cir.1993) ("There is no governmental powers exception to section 362(a)(3)...."). [FN4]

FN4. The Supreme Court's decision in Board of Governors v. MCorp Fin., Inc., 502 U.S. 32, 112 S.Ct. 459, 116 L.Ed.2d 358 (1991) indirectly supports our view. While in bankruptcy, MCorp sought to enjoin two administrative proceedings brought against it by the Federal Reserve Board. Among the arguments MCorp made was that § 362(a)(3) stayed the administrative proceedings. The Supreme Court rejected that argument, not on the ground that (b)(4) did not apply to (a)(3), but on the ground that the automatic stay provisions do not apply to ongoing, nonfinal administrative proceedings.

To sum up, we hold that: the PUC's conduct in reducing the scope of the authority transferred by CPCN 2378 & I was governmental regulatory action under § 362(b)(4); whether § 362(a)(1) or (a)(3) was the stay provision applicable to the PUC's action, in either event, § 362(b)(4) exempted that action from the automatic stay and authorized the Transfer Decision. We therefore AFFIRM the district court's order overturning the injunction issued by the bankruptcy court.

END OF DOCUMENT

In re YORK-HANNOVER DEVELOPMENTS, INC., Debtor.
Richard D. SPARKMAN, Trustee, Plaintiff,
v.
STATE OF FLORIDA DEPARTMENT OF REVENUE, Defendant.

Bankruptcy No. 92-01424-5-ATS.
Adversary No. S-94-00145-5-AP.

United States Bankruptcy Court, E.D. North Carolina,
Raleigh Division.

Oct. 10, 1996.

Chapter 7 trustee sought to recover alleged fraudulent transfers from Florida Department of Revenue. The Bankruptcy Court, A. Thomas Small, Chief Judge, held that: (1) Bankruptcy clause in Article I did not authorize Congress to abrogate state sovereign immunity under Bankruptcy Code, and (2) state did not waive sovereign immunity.

So ordered.

[1] BANKRUPTCY ⚖2679
51k2679
Chapter 7 trustee's causes of action seeking to recover alleged fraudulent transfers from state of Florida were precluded by state's right to sovereign immunity; Bankruptcy Code's abrogation of state sovereign immunity was invalid, and state did not file proof of claim or participate in proceeding and, thus, did not waive sovereign immunity. Bankr.Code, 11 U.S.C.A. § 106(a).

[2] BANKRUPTCY ⚖2679
51k2679
Bankruptcy Clause in Article I did not authorize Congress to abrogate state sovereign immunity under Bankruptcy Code. U.S.C.A. Const.Amend. 11; Bankr.Code, 11 U.S.C.A. § 106(a).

[3] BANKRUPTCY ⚖2679
51k2679
State may waive its sovereign immunity by filing proof of claim or by participating in proceeding.

*138 Richard D. Sparkman, Angier, NC, for Trustee.

Kent L. Weissinger, Assistant General Counsel, Florida Dept. of Revenue, Tallahassee, FL, for State of Florida Dept. of Rev.

Phillip M. Seligman, Civil Division, U.S. Department of Justice, Washington, DC, for U.S.

MEMORANDUM OPINION AND ORDER GRANTING MOTION TO DISMISS

A. THOMAS SMALL, Chief Judge.

This is an adversary proceeding brought by Richard D. Sparkman, chapter 7 trustee for York-Hannover Developments, Inc. ("YHDI"), to recover alleged fraudulent transfers totaling $15,405 from the State of Florida Department of Revenue pursuant to 11 U.S.C. § 548 and the North Carolina fraudulent conveyance statutes pursuant to § 544(b). [FN1] The defendant, the State of Florida, did not file a proof of claim in this case, did not previously participate in this case and has in no way consented to this court's jurisdiction.

FN1. Although the complaint does not provide specific facts as to the alleged nature of the transfers, the debtor apparently paid taxes to the State of Florida on behalf of a related corporation.

The State of Florida filed a motion to dismiss on the grounds of sovereign immunity and a hearing was held in Raleigh, North Carolina on February 22, 1995. Section 106(a) of the Bankruptcy Code, as amended by the Bankruptcy Reform Act of 1994, Pub.L. No. 103-394, § 113, 108 Stat. 4106 (1994), expressly precludes the sovereign immunity defense in this proceeding. [FN2] Section 106(a) provides that "[n]otwithstanding an assertion of sovereign immunity, sovereign immunity is abrogated as to a governmental unit to the extent set forth in this section with respect to the following: (1) Sections ... 544, [and] 548." [FN3]

FN2. The legislative history to the Bankruptcy Reform Act of 1994 clearly states that § 106 was being amended to conform with the Supreme Court's requirement that Congress make an "unmistakably clear" statement of its intent to abrogate States' immunity in the text of the statute.

H.R. REP. No. 103-835, 103d Cong., 2d. Sess., 42 (1994), reprinted in 1994 U.S.C.C.A.N. 3340, 3350-51 (citing Hoffman v. Connecticut Dep't of Income Maintenance, 492 U.S. 96, 109 S.Ct. 2818, 106 L.Ed.2d 76 (1989); Atascadero State Hosp. v. Scanlon, 473 U.S. 234, 242, 105 S.Ct. 3142, 3147, 87 L.Ed.2d 171 (1985)). Congress' intention to abrogate sovereign immunity with respect to claims brought under § 548 and § 544 is clear and only the constitutionality of Congress' authority to so abrogate under the Article I Bankruptcy Clause Power is at issue in this proceeding. Section 702(b)(2)(B) of the Bankruptcy Reform Act of 1994 mandates that § 113 of the Reform Act, codified as 11 U.S.C § 106(a), shall apply retroactively to bankruptcy cases commenced prior to the enactment of the Reform Act. Bankruptcy Reform Act of 1994, Pub.L. No. 103-394 at § 702, 108 Stat. at 4150. The retroactive application of § 106(a) was not disputed in this proceeding.

FN3. The full text of § 106 is as follows:

11 U.S.C. § 106. Waiver of sovereign immunity

(a) Notwithstanding an assertion of sovereign immunity, sovereign immunity is abrogated as to a governmental unit to the extent set forth in this section with respect to the following:

(1) Sections 105, 106, 107, 108, 303, 346, 362, 363, 364, 365, 366, 502, 503, 505, 506, 510, 522, 523, 524, 525, 542, 543, 544, 545, 546, 547, 548, 549, 550, 551, 552, 553, 722, 724, 726, 728, 744, 749, 764, 901, 922, 926, 928, 929, 944, 1107, 1141, 1142, 1143, 1146, 1201, 1203, 1205, 1206, 1227, 1231, 1301, 1303, 1305, and 1327 of this title.

(2) The court may hear and determine any issue arising with respect to the application of such sections to governmental units.

(3) The court may issue against a governmental unit an order, process, or judgment under such sections or the Federal Rules of Bankruptcy Procedure, including an order or judgment awarding a money recovery, but not including an award of punitive damages. Such order or judgment for costs or fees under this title or the Federal Rules of Bankruptcy Procedure against any governmental unit shall be consistent with the provisions and limitations of section 2412(d)(2)(A) of title 28.

(4) The enforcement of any such order, process, or judgment against any governmental unit shall be consistent with appropriate nonbankruptcy law applicable to such governmental unit and, in the case of a money judgment against the United States, shall be paid as if it is a judgment rendered by a district court of the United States.

(5) Nothing in this section shall create any substantive claim for relief or cause of action not otherwise existing under this title, the Federal Rules of Bankruptcy Procedure, or nonbankruptcy law.

(b) A governmental unit that has filed a proof of claim in the case is deemed to have waived sovereign immunity with respect to a claim against such governmental unit that is property of the estate and that arose out of the same transaction or occurrence out of which the claim of such governmental unit arose.

(c) Notwithstanding any assertion of sovereign immunity by a governmental unit, there shall be offset against a claim or interest of a governmental unit any claim against such governmental unit that is property of the estate.

*139 The State of Florida, however, argued that Congress lacked constitutional authority to abrogate state sovereign immunity when legislating pursuant to the Constitution's Article I Bankruptcy Clause [FN4] and that the Eleventh Amendment [FN5] prevented such an abrogation. Mr. Sparkman, the trustee, asserted that in Pennsylvania v. Union Gas Co., 491 U.S. 1, 109 S.Ct. 2273, 105 L.Ed.2d 1 (1989), the Supreme Court recognized Congress' authority to abrogate state sovereign immunity under the Interstate Commerce Clause of Article I and that Congress had similar authority under Article I's Bankruptcy Clause. The State of Florida contended that the Supreme Court was considering similar issues in the then pending case of Seminole Tribe of Florida v. Florida, and that when that case was decided, the Court would overrule Union Gas.

FN4. Article I of the Constitution gives Congress the authority "[t]o establish an uniform Rule of Naturalization, and uniform Laws on the subject of Bankruptcies throughout the United States[.]" U.S. CONST. art. I, § 8, cl. 4.

FN5. The Eleventh Amendment provides: "The Judicial power of the United States shall not be construed to extend to any suit in law or equity, commenced or prosecuted against one of the United States by Citizens of another State, or by Citizens or Subjects of any Foreign State." U.S. CONST. amend. XI.

On April 18, 1995, this court, based on the Seventh Circuit Court of Appeals' decision in McVey Trucking, Inc. v. Secretary of State of Illinois (In re McVey Trucking, Inc.), 812 F.2d 311 (7th

Cir.1987), cert. denied sub nom. Edgar v. McVey Trucking Co., 484 U.S. 895, 108 S.Ct. 227, 98 L.Ed.2d 186 (upholding Congress' authority to abrogate sovereign immunity under the Bankruptcy Clause) and Union Gas, held that Congress acted within its constitutional authority under the Bankruptcy Clause when it amended § 106, and denied the State of Florida's motion to dismiss. Sparkman v. State of Florida Dept. of Revenue (In re York-Hannover Devs., Inc.), 181 B.R. 271 (Bankr.E.D.N.C.1995). The State of Florida appealed to the United States District Court for the Eastern District of North Carolina, and relying on Union Gas, the district court affirmed, holding that "Congress may abrogate the presumption of immunity arising under the Eleventh Amendment when acting pursuant to its Article I powers, including its power to enact uniform bankruptcy laws." State of Florida Dept. of Revenue v. Sparkman (In re York-Hannover Devs., Inc.), 190 B.R. 62, 65 (E.D.N.C.1995).

The State of Florida appealed to the United States Court of Appeals for the Fourth Circuit, and while the appeal was pending, as *140 predicted by the State of Florida, the United States Supreme Court overruled Union Gas in Seminole Tribe of Florida v. Florida, 517 U.S. 44, 116 S.Ct. 1114, 134 L.Ed.2d 252 (1996). The Fourth Circuit Court of Appeals vacated the district court's opinion and remanded this proceeding to the district court for reconsideration. In turn, the district court, on June 20, 1996, remanded the proceeding to this bankruptcy court for reconsideration in light of the Seminole decision. [FN6]

> FN6. See, Ohio Agric. Commodity Depositors Fund v. Mahern, --- U.S. ----, 116 S.Ct. 1411 (1966) (granting certiorari, vacating judgment, and remanding "for further consideration in light of" Seminole in the case of In re Merchants Grain Inc., 59 F.3d 630 (7th Cir.1995)). In Merchants Grain, the Seventh Circuit held that § 106(a) was a constitutional abrogation of the Eleventh Amendment and sovereign immunity under Congress' Bankruptcy Clause power. However, that issue in Merchants Grain appears to have become moot due to the resolution of a related proceeding on other grounds. In re Merchants Grain, Inc. ex rel. Mahern, 93 F.3d 1347 (7th Cir.1996). See also, In re National Cattle Congress, Inc., 91 F.3d 1113 (8th Cir.1996) (remanding for reconsideration in light of Seminole).

A hearing on the remand was conducted by telephone conference call on September 9, 1996, but Mr. Sparkman did not participate and the United States Department of Justice, which had initially intervened to uphold the constitutionality of § 106, was a party to the telephone hearing but did not state a position. While the plaintiff and the United States had no position on the subject, sovereign immunity and the Supreme Court's decision in Seminole have been the subject of considerable discussion and speculation.

In Seminole, the Supreme Court considered whether Congress had acted pursuant to a valid grant of constitutional power when it abrogated state sovereign immunity under its Article I Indian Commerce Clause authority. U.S. CONST., art. I, § 8, cl. 3. The statute at issue in Seminole was the Indian Gaming Regulatory Act, 25 U.S.C.A. §§ 2701-2721 (West Supp.1996), that required States to negotiate in good faith with tribes regarding gaming compacts and permitted tribes to sue States in federal courts to enforce that duty.

Previously, in Pennsylvania v. Union Gas Co., 491 U.S. 1, 109 S.Ct. 2273, 105 L.Ed.2d 1 (1989), the Supreme Court held that Congress could abrogate state sovereign immunity pursuant to the interstate provision of Article I's Commerce Clause. U.S. CONST. art. I, § 8, cl. 3. The decision in Union Gas, however, was a plurality opinion and "a majority of the Court [in Union Gas] expressly disagreed with the rationale of the plurality." Seminole, 517 U.S. at ----, 116 S.Ct. at 1128 (citations omitted).

By a majority of five to four, the Supreme Court in Seminole specifically overruled Union Gas and held that Congress lacked authority under either the Interstate or Indian provisions of the Commerce Clause to avoid state sovereign immunity as embodied in the Eleventh Amendment. Chief Justice Rehnquist, writing for the majority, stated that the Eleventh Amendment and principles of state sovereign immunity embodied in that Amendment, "restrict[ ] the judicial power under Article III, and Article I cannot be used to circumvent the constitutional limitations [thus] placed upon federal jurisdiction." Seminole, 517 U.S. at ---- - ----, 116 S.Ct. at 1131-32.

[1] The State of Florida now argues that if Congress cannot abrogate state sovereign immunity under Article I's Interstate Commerce Clause or the Indian Commerce Clause, it may not do so under Article I's Bankruptcy Clause. This court agrees. Just as the Supreme Court found that there is "no principled distinction in favor of the States to be drawn between the Indian Commerce Clause and the Interstate Commerce Clause[,]" Seminole, 517 U.S. at ----, 116 S.Ct. at 1127, this court can find no difference, with respect to Congress' Article I powers, between the Bankruptcy Clause and the Interstate Commerce Clause or the Indian Commerce Clause. The fact that bankruptcy law is federal law exclusively within the province of Congress does not make the Bankruptcy Clause different. The Supreme Court was quite clear in that regard. "[T]he background principle of state sovereign immunity embodied in the Eleventh Amendment is not so ephemeral as to dissipate when the subject of the suit is an area, like ***141** the regulation of Indian commerce, that is under the exclusive control of the Federal Government." Seminole, 517 U.S. at ----, 116 S.Ct. at 1131. Under Seminole, state governments that receive avoidable transfers may receive better treatment than other transferees, but "[p]resumably the Supreme Court would opine that this lack of equality is the price we must pay for the Constitution's continuing recognition of the sovereignty of the states." S. Elizabeth Gibson, Sovereign Immunity in Bankruptcy: The Next Chapter, 70 AM.BANKR. L.J. 195, 202 (1996) (citing Seminole).

[2] Consequently, the court now concludes, as have other courts that have considered the issue, that the Bankruptcy Clause in Article I does not authorize Congress to abrogate state sovereign immunity and, specifically, that the Bankruptcy Clause did not authorize Congress to abrogate state sovereign immunity under 11 U.S.C. § 106(a). In re Martinez, 196 B.R. 225 (D.P.R.1996); Ellenberg v. Board of Regents (In re Midland Mechanical Contractors, Inc.), 200 B.R. 453 (Bankr.N.D.Ga.1996); Burke v. State of Ga. ex rel. Department of Revenue (In re Burke), 200 B.R. 282 (Bankr.S.D.Ga.1996); Schulman v. California State Water Resources Control Bd. (In re Lazar), 200 B.R. 358 (Bankr.C.D.Cal.1996); and In re Sacred Heart Hosp., 199 B.R. 129 (Bankr.E.D.Pa.1996).

Although not argued in this proceeding, it has been suggested that Congress had constitutional authority, other than pursuant to Article I, to enact § 106(a) and to abrogate state sovereign immunity.

In Seminole, the Court recognized that Congress may abrogate state sovereign immunity when acting pursuant to § 5 of the Fourteenth Amendment. [FN7] Seminole 517 U.S. at ----, 116 S.Ct. at 1128 (citing Fitzpatrick v. Bitzer, 427 U.S. 445, 96 S.Ct. 2666, 49 L.Ed.2d 614 (1976)). This power had previously been upheld in Fitzpatrick v. Bitzer, 427 U.S. 445, 96 S.Ct. 2666, 49 L.Ed.2d 614 (1976), where the Court noted that the Fourteenth Amendment was adopted well after both the Eleventh Amendment and the States' ratification of the Constitution, thus allowing the Fourteenth Amendment "to alter the pre-existing balance between state and federal power achieved by Article III and the Eleventh Amendment." Seminole, 517 U.S. at ----, 116 S.Ct. at 1128 (citing Fitzpatrick, 427 U.S. 445, 96 S.Ct. 2666, 49 L.Ed.2d 614 (1976)).

> FN7. Section 5 of the Fourteenth Amendment provides that "[t]he Congress shall have power to enforce, by appropriate legislation, the provisions of this article." U.S. CONST. amend. XIV. Section 1 of the Fourteenth Amendment provides, in pertinent part, that "[n]o State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any State deprive any person of life, liberty, or property, without due process of law; nor deny any person within its jurisdiction the equal protection of the laws." U.S. CONST. amend. XIV.

Prior to the Supreme Court's decision in Seminole, Chief Bankruptcy Judge Mickey Dan Wilson of the United States Bankruptcy Court for the Eastern District of Oklahoma, in Mather v. Oklahoma Employment Sec. Comm'n (In re Southern Star Foods, Inc.), 190 B.R. 419 (Bankr.E.D.Okla.1995), held that Congress was authorized to enact § 106(a) under § 5 of the Fourteenth Amendment. Judge Wilson reasoned that:

> Congress' exercise of its basic national legislative powers under any of the provisions of Article I will usually ... implicate 'the privileges or immunities of the citizens of the United States ... life, liberty, or property ... due process of law ... [or] the equal protection of the laws.' A State

> cannot limit the exercise by a citizen of the United States of a right conferred by a valid act of Congress. Article I of the Constitution gives the national government power to legislate on the subject of bankruptcy; and the national government has done so, by creating the complex of privileges and immunities, rights and liabilities, found in the Bankruptcy Code.

Star Foods, 190 B.R. at 426 (citation omitted). Judge Wilson concluded that although the bankruptcy laws "are enacted 'pursuant to Article I,' they are enforceable 'through the Fourteenth Amendment' [because] to separate the power of national enactment under Article I from the power of national *142 enforcement under the Fourteenth Amendment is to mince the Constitution ... and dismember it into a scatter of lifeless parts." Id. The holding of Star Foods was recently adopted by Bankruptcy Judge John S. Dalis in Headrick v. State of Georgia, ex rel. Department of Revenue (In re Headrick), 200 B.R. 963 (Bankr.S.D.Ga.1996).

However, the issue of Congress' authority to abrogate States' sovereign immunity under § 5 of the Fourteenth Amendment is not before the court in this proceeding and in light of Seminole, the court concludes that Congress did not act within its constitutional authority when enacting § 106(a). Furthermore, there do not appear to be any other grounds to preclude the State of Florida's sovereign immunity defense. It could be argued that since the plaintiff here is a bankruptcy trustee, sovereign immunity does not apply because the suit was brought by a federal official. But, as one court has held, that is "an implausible construction of the role of the trustee." Schulman v. California State Water Resources Control Bd. (In re Lazar), 200 B.R. 358 (Bankr.C.D.Cal.1996). [FN8]

> FN8. It has been argued that sovereign immunity might not apply if the United States Trustee brought the proceeding, but this seems equally implausible. Harvard Professor Offers Possible Response to Seminole, BANKRUPTCY COURT DECISIONS WEEKLY NEWS AND COMMENT, August 20, 1996, at A6.

[3] A State may waive its sovereign immunity by filing a proof of claim or by participating in the proceeding. Schulman v. California State Water Resources Control Bd. (In re Lazar), 200 B.R. 358 (Bankr.C.D.Cal.1996), In re Sacred Heart Hosp., 199 B.R. 129 (Bankr.E.D.Pa.1996), Burke v. State of Ga. ex rel. Department of Revenue (In re Burke), 200 B.R. 282 (Bankr.S.D.Ga.1996). The State of Florida, however, has neither filed a proof of claim nor participated in this proceeding in any way.

Based on the foregoing, the plaintiff's causes of action in this federal court are precluded by the State of Florida's right to sovereign immunity, and this adversary proceeding is DISMISSED. [FN9] A separate judgment will be entered.

> FN9. It has been suggested that while a trustee may not pursue a § 548 action against a State in a federal forum, a trustee may be able to bring an action in state court. See S. Elizabeth Gibson, Sovereign Immunity in Bankruptcy: The Next Chapter, 70 AM.BANKR. L.J. 195, 203-08 (1996).

SO ORDERED.

JUDGMENT

The motion to dismiss this adversary proceeding, filed by the defendant, State of Florida Department of Revenue, was heard by telephone conference call on September 9, 1996, pursuant to the remand order entered by the United States District Court for the Eastern District of North Carolina on June 20, 1996. The basis for this court's ruling is set forth in a Memorandum Opinion and Order entered this date. Based on that ruling,

IT IS HEREBY ORDERED, ADJUDGED, AND DECREED that this adversary proceeding against the defendant, State of Florida Department of Revenue, is DISMISSED.

END OF DOCUMENT

In re Tamra M. KOEHLER, Debtor.
Tamra M. KOEHLER, Plaintiff,
v.
IOWA COLLEGE STUDENT AID COMMISSION, Defendant.
Tamra M. KOEHLER, Plaintiff,
v.
NATIONAL CREDIT SERVICES CORP., Defendant.

Bankruptcy No. 4-94-6040.
Adv. No. 4-96-0087.

United States Bankruptcy Court,
D. Minnesota.

Jan. 6, 1997.

Discharged Chapter 13 debtor brought adversary proceeding against Iowa College Student Aid Commission (ICSAC), seeking declaration that student loan was discharged, and monetary damages for automatic stay violations. Commission filed counterclaim for loan balance plus collection costs, and moved to dismiss debtor's damages count for lack of subject matter jurisdiction. The Bankruptcy Court, Nancy C. Dreher, J., held that: (1) Bankruptcy Code sovereign immunity waiver was unconstitutional as applied to unconsenting state; (2) Commission did not waive sovereign immunity under Bankruptcy Code, since it failed to file claim in Chapter 13 case; but (3) Commission waived Eleventh Amendment immunity to extent that debtor's damages would be equal to or less than counterclaim for underlying debt.

Motion denied.

[1] FEDERAL COURTS ⚖265
170Bk265
Notwithstanding assertion of Eleventh Amendment immunity, federal court may exercise jurisdiction over suit for damages between individual and state if Congress has validly abrogated state's sovereign immunity, or state has voluntarily waived its sovereign immunity. U.S.C.A. Const.Amend. 11.

[2] FEDERAL COURTS ⚖265
170Bk265
Congress, under Fourteenth Amendment, has power to abrogate state's Eleventh Amendment immunity by making its intention to do so unmistakably clear in language of statute. U.S.C.A. Const.Amends. 11, 14, § 5.

[3] BANKRUPTCY ⚖2679
51k2679
Bankruptcy Code sovereign immunity abrogation provision is unconstitutional insofar as it attempts to abrogate unconsenting state's sovereign immunity from suit in federal court. U.S.C.A. Const. Art. 1, § 8, cls. 3, 4; Amend. 11; Bankr.Code, 11 U.S.C.A. § 106(a).

[4] BANKRUPTCY ⚖2679
51k2679
Congress may not attempt to abrogate states' Eleventh Amendment immunity using powers granted to it under bankruptcy clause of Article I. U.S.C.A. Const. Art. 1, § 8, cl. 4; Amend. 11.

[5] BANKRUPTCY ⚖2679
51k2679
Because of Eleventh Amendment, Bankruptcy Code's general abrogation of sovereign immunity did not effectively abrogate Iowa College Student Aid Commission's (ICSAC) Eleventh Amendment immunity and provided no predicate for assertion of federal subject matter jurisdiction over Chapter 13 debtor's cause of action seeking damages for ICSAC's alleged willful violations of automatic stay. U.S.C.A. Const.Amend. 11; Bankr.Code, 11 U.S.C.A. §§ 106(a), 362.

[6] FEDERAL COURTS ⚖267
170Bk267
If state voluntarily waives its sovereign immunity by consenting to be sued in federal court, Eleventh Amendment will not bar action. U.S.C.A. Const.Amend. 11.

[7] FEDERAL COURTS ⚖266.1
170Bk266.1
Where state has legislated on subject of waiver of immunity to suit in federal court, state will be deemed to have waived its immunity only where it has stated its intention to waive by most express language or by such overwhelming implication from text as will leave no room for any other reasonable construction. U.S.C.A. Const.Amend. 11.

[8] FEDERAL COURTS ⚖267

170Bk267
In absence of explicit consent by state statute or constitutional provision, state's consent to be sued in federal court may be constitutionally inferred through its affirmative conduct. U.S.C.A. Const.Amend. 11.

[9] FEDERAL COURTS ⚿267
170Bk267
For explicit waiver of Eleventh Amendment immunity to be found, state must, by legislation or constitutional provision, expressly consent to be sued in federal court, not merely to be sued in any court of competent jurisdiction or to be sued in its own state courts; instead, statute or constitutional provision must unequivocally specify state's intention to subject itself to suit in federal court. U.S.C.A. Const.Amend. 11.

[10] FEDERAL COURTS ⚿266.1
170Bk266.1
Federal statute may be used to waive state's Eleventh Amendment immunity as long as Congress had indicated clear and unmistakable intent to make states liable in federal court if they engaged in particular activity, and state then voluntarily chooses to engage in that conduct. U.S.C.A. Const.Amend. 11.

[11] FEDERAL COURTS ⚿267
170Bk267
Constructive waiver of state's Eleventh Amendment immunity may be found only where there exists unequivocal indication that state intends to consent to federal jurisdiction that would otherwise be barred by Eleventh Amendment. U.S.C.A. Const.Amend. 11.

[12] FEDERAL COURTS ⚿266.1
170Bk266.1
Once state waives its Eleventh Amendment immunity in particular case, such action cannot ordinarily be undone. U.S.C.A. Const.Amend. 11.

[13] FEDERAL COURTS ⚿266.1
170Bk266.1
Although Attorney General of Iowa does not possess authority to waive Iowa's sovereign immunity merely by making general appearance in federal court, Attorney General has authority to waive Iowa's immunity by bringing claim in federal court. U.S.C.A. Const.Amend. 11; I.C.A. § 13.2, subd. 2.

[14] BANKRUPTCY ⚿2679
51k2679
Bankruptcy Code state sovereign immunity waiver provision did not apply to Iowa College Student Aid Commission's (ICSAC) counterclaim in Chapter 13 debtor's adversary proceeding for stay violations, where Commission did not file proof of claim in Chapter 13 case. Bankr.Code, 11 U.S.C.A. § 106(b, c).

[15] FEDERAL COURTS ⚿266.1
170Bk266.1
When state takes affirmative action to recover on claim in federal court, state waives its Eleventh Amendment immunity with respect to any counterclaims that arise out of same transaction or occurrence as state's claim, i.e., with respect to any compulsory counterclaims asserted against state. U.S.C.A. Const.Amend. 11.

[16] FEDERAL COURTS ⚿266.1
170Bk266.1
Under "recoupment theory" of Eleventh Amendment immunity waiver, state's waiver is limited in scope to those counterclaims asserted for purpose of defeating or diminishing state's recovery, and no affirmative recovery against state is permitted. U.S.C.A. Const.Amend. 11.

[17] BANKRUPTCY ⚿2679
51k2679
Iowa College Student Aid Commission's (ICSAC) counterclaim in Chapter 13 debtor's automatic stay violation proceeding was affirmative action, which waived Commission's Eleventh Amendment immunity just as if Commission had filed complaint, to extent that debtor's claim diminished Commission's counterclaim, but would not allow debtor affirmative recovery. U.S.C.A. Const.Amend. 11.

[18] FEDERAL COURTS ⚿266.1
170Bk266.1
For purposes of Eleventh Amendment immunity, unlike mere general appearance by state in federal court, filing of counterclaim constitutes affirmative conduct on part of state and is thus significantly more than simple appearance in court for purpose of defending on the merits or for limited purpose of contesting jurisdiction. U.S.C.A. Const.Amend.

11.

[19] FEDERAL CIVIL PROCEDURE ⚖775.1
170Ak775.1
When identifying compulsory counterclaims, determination of whether competing claims arise out of same transaction or occurrence is made by considering one or more of four factors: (1) are issues of fact and law raised by claim and counterclaim largely the same? (2) would res judicata bar subsequent suit on defendant's claim absent compulsory counterclaim rule? (3) will substantially same evidence support or refute plaintiff's claim as well as defendant's counterclaim? and (4) is there any logical relation between claim and counterclaim? Fed.Rules Civ.Proc.Rule 13(a), 28 U.S.C.A.

[20] BANKRUPTCY ⚖2461
51k2461
Automatic stay violation claim against governmental unit is likely related to governmental unit's claim for recovery of underlying debt, for purposes of determining whether sovereign immunity has been waived. Bankr.Code, 11 U.S.C.A. § 362(h).

[20] BANKRUPTCY ⚖2679
51k2679
Automatic stay violation claim against governmental unit is likely related to governmental unit's claim for recovery of underlying debt, for purposes of determining whether sovereign immunity has been waived. Bankr.Code, 11 U.S.C.A. § 362(h).

*212 Russell A. Norum, Wayzata, MN, for plaintiff.

Daniel S. Rabin, Berman, Singer & Rabin, P.A., Overland Park, KS, Rodney A. Honkanen, Wagner, Falconer & Judd, Ltd., Minneapolis, MN, for defendant National Credit Service Corp.

Janet S. Wisby, Assistant Attorney General, Des Moines, IA, for defendant ICSAC.

*213 ORDER DENYING DEFENDANT'S MOTION TO DISMISS COUNT TWO OF PLAINTIFF'S COMPLAINT

NANCY C. DREHER, Bankruptcy Judge.

The above-entitled matter came on for hearing before the undersigned on the motion of Defendant, Iowa College Student Aid Commission (ICSAC), to dismiss Count Two of the Plaintiff's Complaint due to lack of subject matter jurisdiction under the sovereign immunity doctrine of the Eleventh Amendment to the United States Constitution. In light of the recent United States Supreme Court decision in Seminole Tribe of Florida v. Florida, --- U.S. ----, 116 S.Ct. 1114, 134 L.Ed.2d 252 (1996), the parties were asked to brief the issue of the effect of the Eleventh Amendment on this Court's jurisdiction over Count Two of the Plaintiff's Complaint. After carefully considering the arguments of counsel, I hold that ICSAC has waived its Eleventh Amendment sovereign immunity by filing a counterclaim in this proceeding, that this Court does not lack subject matter jurisdiction over Count Two, and that Defendant's motion to dismiss Count Two should be denied.

FACTS

Tamra M. Koehler (Plaintiff) is a resident of the State of Minnesota. Between October, 1981 and August, 1984, the Plaintiff executed a series of promissory notes totaling $10,000 in principal amount in exchange for student loans received under a government-funded student loan program. ICSAC is an agency of the State of Iowa authorized under Iowa law to administer and enforce the Iowa Guaranteed Loan Program which served as guarantor of the Plaintiff's loans. Plaintiff defaulted on her obligation to repay the loans. Subsequently, ICSAC paid the debt pursuant to the terms of its guaranty and the notes were endorsed and assigned to ICSAC for collection.

On December 1, 1994, the Plaintiff filed a petition for relief under Chapter 13 of the United States Bankruptcy Code. Neither ICSAC nor the Plaintiff filed a proof of claim on behalf of ICSAC in the Chapter 13 case. During the case, ICSAC allegedly made attempts to collect the loans in willful violation of the automatic stay. Plaintiff's Chapter 13 plan was confirmed on February 3, 1995. After paying 100 percent of the filed claims under the Chapter 13 Plan, the Plaintiff received a discharge on February 2, 1996.

On March 29, 1996, the Plaintiff commenced the current adversary proceeding. In Count One of her Complaint, Plaintiff seeks a declaration that the debt

to ICSAC was discharged. In Count Two, Plaintiff seeks monetary damages against ICSAC for alleged willful violations of the automatic stay.

On behalf of ICSAC, the Attorney General for the State of Iowa filed an Answer to the Plaintiff's Complaint and a Counterclaim for judgment in the amount of $13,706.39, the unpaid principal and interest balance of the loans, plus collection costs. ICSAC then moved to dismiss Count Two of the Complaint, arguing that the Bankruptcy Court lacks subject matter jurisdiction under the sovereign immunity doctrine of the Eleventh Amendment. [FN1] The issue to be decided is whether and to what extent ICSAC has waived its Eleventh Amendment immunity against suit for damages by filing a counterclaim seeking judgment for the debt.

FN1. ICSAC does not assert that this Court lacks subject matter jurisdiction over Count One of the Complaint, which seeks prospective declaratory relief. See Ex Parte Young, 209 U.S. 123, 28 S.Ct. 441, 52 L.Ed. 714 (1908) (prospective injunctive relief available against state officials).

DECISION

I. THE ELEVENTH AMENDMENT

The Eleventh Amendment to the United States Constitution provides: "The Judicial power of the United States shall not be construed to extend to any suit in law or equity, commenced or prosecuted against one of the United States by Citizens of another State, or by Citizens or Subjects of any Foreign State." [FN2] Prior to the ratification of the Constitution, *214 it was widely understood that the common-law principle of sovereign immunity would prevent Article III's grant of federal judicial power from making states unwilling defendants in federal court. Employees v. Missouri Dep't of Pub. Health and Welfare, 411 U.S. 279, 291-92, 93 S.Ct. 1614, 1621, 36 L.Ed.2d 251 (1973) (Marshall, J., concurring). "Because of the problems of federalism inherent in making one sovereign appear against its will in the courts of the other, a restriction upon the exercise of the federal judicial power has long been considered appropriate...." Id. at 294, 93 S.Ct. at 1622-23. The Eleventh Amendment was added to the Constitution in 1798 to affirm the Framers' original intent that "the fundamental principle of sovereign immunity limits the grant of judicial authority in Art. III." Pennhurst State Sch. & Hosp. v. Halderman, 465 U.S. 89, 98, 104 S.Ct. 900, 906-07, 79 L.Ed.2d 67 (1984). Therefore, by restricting the grant of judicial power found in Article III, the Eleventh Amendment represents a constitutional limitation on the subject matter jurisdiction of the federal courts. Id.

FN2. While the language of the Eleventh Amendment rather clearly limits a state's immunity from suit to situations where the state has been sued by a non-resident, it has not been so interpreted. Long ago, this language was interpreted to preclude suits brought against the state by any individual, whether a resident of the state or not. Hans v. Louisiana, 134 U.S. 1, 10 S.Ct. 504, 33 L.Ed. 842 (1890).

[1] In this case, the Plaintiff, a resident of the State of Minnesota, has commenced an adversary proceeding seeking damages against ICSAC, an agency of the State of Iowa. It is immediately apparent that the language of the Eleventh Amendment purports to foreclose federal subject matter jurisdiction over Count Two of the Plaintiff's Complaint by its very terms. There are two recognized exceptions to the reach of the Eleventh Amendment, however. Notwithstanding an assertion of Eleventh Amendment immunity, a federal court may exercise jurisdiction over a suit for damages between an individual and a state if: 1) Congress has validly abrogated the state's sovereign immunity; or 2) the state has voluntarily waived its sovereign immunity. Pennhurst State Sch. & Hosp., 465 U.S. at 99, 104 S.Ct. at 907-08.

II. CONGRESSIONAL ABROGATION IN SECTION 106(a)

[2] The first exception to the reach of the Eleventh Amendment which must be considered is the doctrine of congressional abrogation. It is well-established that Congress, under § 5 of the Fourteenth Amendment, has the power to abrogate a state's Eleventh Amendment immunity by making its intention to do so "unmistakably clear in the language of the statute." Blatchford v. Native Village of Noatak, 501 U.S. 775, 786, 111 S.Ct. 2578, 2584-85, 115 L.Ed.2d 686 (1991); Dellmuth v. Muth, 491 U.S. 223, 227-28, 109 S.Ct. 2397, 2400, 105 L.Ed.2d 181 (1989); Fitzpatrick v. Bitzer, 427 U.S. 445, 456, 96 S.Ct. 2666, 2671, 49 L.Ed.2d 614 (1976).

In 1994, former § 106(c), [FN3] now § 106(a), of the United States Bankruptcy Code was amended to make Congress' intention clear in this regard. In clear and unmistakable language, current § 106(a) purports to abrogate the sovereign immunity of any "governmental unit," including that of a state, [FN4] for actions arising out of § 362 of the Bankruptcy Code. [FN5] The amendment was enacted to address the Supreme Court's decisions in United States v. Nordic Village, Inc., 503 U.S. 30, 112 S.Ct. 1011, 117 L.Ed.2d 181 (1992), and Hoffman v. Conn. Dep't of Income Maintenance, 492 U.S. 96, 109 S.Ct. 2818, 106 L.Ed.2d 76 (1989). Under the rulings in those cases, an earlier and less specifically-worded version of current § 106(a) was found to be an insufficiently clear expression of congressional intent to ***215** abrogate the sovereign immunity of the states and the federal government. See Nordic Village, 503 U.S. at 34, 112 S.Ct. at 1015; Hoffman, 492 U.S. at 104, 109 S.Ct. at 2824.

FN3. 11 U.S.C. § 106(c) (1988).

FN4. Section 101(27) provides:
"government unit" means United States; State; Commonwealth; District; Territory; municipality; foreign state; department, agency, or instrumentality of the United States (but not a United States trustee while serving as a trustee in a case under this title), a State, a Commonwealth, a District, a Territory, a municipality, or a foreign state; or other foreign or domestic government. 11 U.S.C. § 101(27) (1994).

FN5. Section 106(a) provides, in relevant part:
"Notwithstanding an assertion of sovereign immunity, sovereign immunity is abrogated as to a governmental unit to the extent set forth in this section with respect to the following: (1) Sections ... 362,...."
11 U.S.C. § 106(a) (1994).

[3][4][5] Almost immediately following the 1994 Amendments, commentators questioned the constitutionality of new § 106(a) as applied to a state's Eleventh Amendment sovereign immunity. [FN6] The Supreme Court's answer to these questions was not long in coming. In Seminole Tribe of Florida v. Florida, --- U.S. ----, 116 S.Ct. 1114, 134 L.Ed.2d 252 (1996), the Supreme Court held that Congress may not use its Article I powers to abrogate a state's Eleventh Amendment immunity. The Seminole decision arose in the context of congressional action taken under Article I, Section 8, clause 3 of the Constitution, the Indian Commerce Clause. The power given to Congress "to establish uniform Laws on the subject of Bankruptcies throughout the United States" is also an Article I power. U.S. Const. art. I, § 8, cl. 4. With near uniformity, [FN7] the commentaries written and the cases decided since Seminole have concluded that it follows from Seminole that § 106(a) is unconstitutional insofar as it attempts to abrogate an unconsenting state's sovereign immunity from suit in federal court. [FN8] This Court agrees. The Seminole decision goes well beyond the Indian Commerce Clause and acts to frustrate any congressional attempt to abrogate Eleventh Amendment immunity using the powers granted to it under the Bankruptcy Clause of Article I. [FN9] Thus, ***216** § 106(a) does not effectively abrogate ICSAC's Eleventh Amendment immunity, and it provides no predicate for an assertion of subject matter jurisdiction over Count Two of the Plaintiff's Complaint.

FN6. See, e.g., S. Elizabeth Gibson, Congressional Response to Hoffman and Nordic Village: Amended Section 106 and Sovereign Immunity, 69 AM.BANKR. L.J. 311 (1995) [hereinafter Gibson I].

FN7. See Headrick v. Georgia (In re Headrick), 200 B.R. 963 (Bankr.S.D.Ga.1996); Burke v. Georgia (In re Burke), 203 B.R. 493 (Bankr.S.D.Ga.1996). In these cases, the United States Bankruptcy Court for the Southern District of Georgia held that Congress can abrogate a state's sovereign immunity in the bankruptcy context because bankruptcy laws passed pursuant to Article I are enforceable as privileges and immunities of the citizens of the United States under the Fourteenth Amendment. See also Mather v. Okla. Employment Sec. Comm'n (In re Southern Star Foods, Inc.), 190 B.R. 419 (Bankr.E.D.Okla.1995) (stating that Article I gives Congress the power to legislate on the subject of bankruptcy, and the Fourteenth Amendment allows debtors to enforce the provisions of the Bankruptcy Code in federal court notwithstanding the states' Eleventh Amendment immunity).

FN8. See Ohio Agric. Commodity Depositors Fund v. Mahern, --- U.S. ----, 116 S.Ct. 1411, 134 L.Ed.2d 537 (1996) (vacating and remanding for further consideration Matter of Merchants Grain, 59 F.3d 630 (7th Cir.1995), which held that Congress had authority under the Bankruptcy

Clause to abrogate Eleventh Amendment immunity); Nat'l Cattle Congress, Inc. v. Iowa Racing and Gaming Comm'n. (In re Nat'l Cattle Congress, Inc.), 91 F.3d 1113, 1114 (8th Cir.1996) (automatic stay violation damage action against state reversed and remanded in light of Seminole); Light v. State Bar of Cal. (In re Light), 1996 WL 341112, *2 (9th Cir.1996) (stating that Seminole forecloses any argument that § 106 abrogates Eleventh Amendment immunity); In re Martinez, 196 B.R. 225, 230 (D.P.R.1996) (finding that § 106 is unconstitutional to the extent it purports to apply to state and commonwealth governments); Sparkman v. Florida (In re York-Hannover Dev., Inc.), 201 B.R. 137 (Bankr.E.D.N.C.1996) (concluding that the Bankruptcy Clause does not authorize Congress to abrogate state sovereign immunity in § 106(a)); Ellenberg v. Bd. of Regents (Matter of Midland Mechanical Contractors, Inc.), 200 B.R. 453 (Bankr.N.D.Ga.1996) (abrogation of Eleventh Amendment immunity found in § 106 has no validity in the wake of Seminole); Schulman v. Cal. State Water Resources Control Bd. (In re Lazar), 200 B.R. 358 (Bankr.C.D.Cal.1996) (discussing the broad reach of the Seminole decision); Sacred Heart Hosp. of Norristown v. Pennsylvania (In re Sacred Heart Hosp. of Norristown), 199 B.R. 129, 134 (Bankr.E.D.Pa.1996) (stating that the Seminole decision is meant to pertain to § 106 of the Bankruptcy Code). See also S. Elizabeth Gibson, Sovereign Immunity in Bankruptcy: The Next Chapter, 70 AM.BANKR. L.J. 195, 201-03 (1996); Russell Dees, Seminole Sovereign Immunity: It's Worse Than You Thought, NORTON BANKRUPTCY LAW ADVISER, Sept. 1996; Karen Cordry, A Tale of Two Sovereigns: Will the Bankruptcy Code Survive Seminole, NORTON BANKRUPTCY LAW ADVISER, May 1996.

FN9. As stated by Justice Stevens in his dissent:

The importance of the majority's decision to overrule the Court's holding in Pennsylvania v. Union Gas Co. [491 U.S. 1, 109 S.Ct. 2273, 105 L.Ed.2d 1 (1989)] cannot be overstated. The majority's opinion does not simply preclude Congress from establishing the rather curious statutory scheme under which Indian tribes may seek the aid of a federal court to secure a State's good faith negotiations over gaming regulations. Rather, it prevents Congress from providing a federal forum for a broad range of actions against States, from those sounding in copyright and patent law, to those concerning bankruptcy, environmental law, and the regulation of our vast national economy.

Seminole, at ----, 116 S.Ct. at 1134 (Stevens, J., dissenting) (emphasis added). Indeed, the Seminole majority's response to this criticism was not to dispute its conclusion, but instead to downplay its significance:

[Justice Stevens'] conclusion is exaggerated both in its substance and in its significance. First, Justice Stevens' statement is misleadingly overbroad. We have already seen that several avenues remain open for ensuring state compliance with federal law. Most notably, an individual may obtain injunctive relief under Ex parte Young in order to remedy a state officer's ongoing violation of federal law. Second, contrary to the implication of Justice Stevens' conclusion, it has not been widely thought that the federal antitrust, bankruptcy, or copyright statutes abrogated the States' sovereign immunity. This Court has never awarded relief against a State under any of those statutory schemes.... Although the copyright and bankruptcy laws have existed practically since our nation's inception ... there is no established tradition in the lower federal courts of allowing enforcement of those federal statutes against the States.

Id., at ---- - ---- n. 16, 116 S.Ct. at 1131-32 n. 16. (citations omitted).

III. CONSTRUCTIVE WAIVER UNDER SECTIONS 106(b) AND (c)

[6][7] The second exception to the Eleventh Amendment's doctrine of sovereign immunity is waiver. In spite of its broad reading of the reach of the Eleventh Amendment, the Supreme Court has consistently adhered to the well- established rule that a consenting state may be sued for damages by an individual in federal court. Atascadero State Hosp. v. Scanlon, 473 U.S. 234, 238, 105 S.Ct. 3142, 3145, 87 L.Ed.2d 171 (1985). See Seminole, at ---- , 116 S.Ct. at 1131 n. 14 ("[T]his Court is empowered to review a question of federal law arising from a state court decision where a State has consented to suit ..."). Therefore, if a state voluntarily waives its sovereign immunity by consenting to be sued in federal court, the Eleventh Amendment will not bar the action. The test used to determine whether a state has waived its immunity is a stringent one, however. Atascadero State Hosp., 473 U.S. at 241, 105 S.Ct. at 3146. Where a state has legislated on the subject, a state will be deemed to have waived its immunity only where it has stated its intention to waive "by the most express language or by such overwhelming implication from the text as will leave no room for any other reasonable construction." Edelman v. Jordan, 415 U.S. 651,

673, 94 S.Ct. 1347, 1361, 39 L.Ed.2d 662 (1974) (quoting Murray v. Wilson Distilling Co., 213 U.S. 151, 171, 29 S.Ct. 458, 464, 53 L.Ed. 742 (1909)).

[8][9] In the absence of explicit consent by state statute or constitutional provision, [FN10] a state's consent to be sued in federal court may be constructively inferred through its affirmative conduct. Clark v. Barnard, 108 U.S. 436, 448, 2 S.Ct. 878, 883, 27 L.Ed. 780 (1883); Hankins v. Finnel, 964 F.2d 853, 856 (8th Cir.1992); Garrity v. Sununu, 752 F.2d 727, 738 (1st Cir.1984). In the history of Eleventh Amendment jurisprudence, it is generally recognized that the doctrine of constructive waiver inferred from conduct reached its outer limits in the Supreme Court case of Parden v. Terminal Railway of Alabama Docks Dep't., 377 U.S. 184, 84 S.Ct. 1207, 12 L.Ed.2d 233 (1964). In Parden, the Supreme Court considered the question of whether the operation of a state-owned railroad by the State of Alabama constituted consent to be sued in federal court under the Federal Employers' Liability Act *217 (FELA). The language of the FELA provided that "[e]very common carrier by railroad while engaging in commerce between any of the several States ... shall be liable in damages to any person suffering injury while he is employed by such carrier in such commerce," and that "[u]nder this chapter an action may be brought in a district court of the United States...." Parden, 377 U.S. at 184; 84 S.Ct. at 1207. In the absence of an express statutory provision to the contrary, the Parden Court interpreted the general language of the FELA to indicate a congressional intent to include participating states within the full coverage of the Act. See id. at 189- 90, 84 S.Ct. at 1211. The Court then concluded that "when [Alabama] began operation of an interstate railroad approximately 20 years after the enactment of the FELA, [it] necessarily consented to such suit as was authorized by that Act." Id. at 191, 84 S.Ct. at 1212.

> FN10. For an explicit waiver of Eleventh Amendment immunity to be found, a state must, by legislation or constitutional provision, expressly consent to be sued in federal court. Neither a state's consent to be sued "in any court of competent jurisdiction" nor its consent to be sued in its own state courts is sufficient to constitute a waiver of Eleventh Amendment immunity. Atascadero State Hosp., 473 U.S. at 241, 105 S.Ct. at 3146; Florida Dept. of Health v. Florida Nursing Home Assn., 450 U.S. 147, 149-150, 101 S.Ct. 1032, 1034, 67 L.Ed.2d 132 (1981) (per curiam). Instead, to constitute a waiver, a state statute or constitutional provision must unequivocally specify the State's intention to subject itself to suit in federal court. Atascadero State Hosp., 473 U.S. at 241, 105 S.Ct. at 3146-47. In this case, the Plaintiff has identified no Iowa statute or Iowa constitutional provision that would satisfy this test, and this Court finds none. Any argument that ICSAC has explicitly waived its Eleventh Amendment sovereign immunity must, therefore, fail.

Twenty-three years later, after a series of cases adhering to the rule that a state will be deemed to have waived its sovereign immunity only where unequivocally stated, [FN11] the Supreme Court ultimately overruled Parden in Welch v. Texas Dep't of Highways & Pub. Transp., 483 U.S. 468, 107 S.Ct. 2941, 97 L.Ed.2d 389 (1987). In Welch, the issue before the Court was whether the language of a federal statute, the Jones Act, was sufficient to authorize suits against the State of Texas in federal court. The language of the Jones Act provided that:

> FN11. See Atascadero State Hosp. v. Scanlon, 473 U.S. 234, 105 S.Ct. 3142, 87 L.Ed.2d 171 (1985); Pennhurst State Sch. & Hosp. v. Halderman, 465 U.S. 89, 104 S.Ct. 900, 79 L.Ed.2d 67 (1984); Fla. Dep't of Health v. Fla. Nursing Home Ass'n, 450 U.S. 147, 101 S.Ct. 1032, 67 L.Ed.2d 132 (1981); Edelman v. Jordan, 415 U.S. 651, 94 S.Ct. 1347, 39 L.Ed.2d 662 (1974).

> Any seaman who shall suffer personal injury in the course of his employment may, at his election, maintain an action for damages at law, with the right of trial by jury, and in such action all statutes of the United States modifying or extending the common-law right or remedy in cases of personal injury to railway employees shall apply.... Jurisdiction in such actions shall be under the court of the district in which the defendant employer resides or in which his principal office is located.

Id. at 470, 107 S.Ct. at 2944 n. 1. The Welch Court held that the general language of the Jones Act was insufficient to authorize suits against states in federal court. In so holding, the Court stated that Congress had not expressed "in unmistakable statutory language its intention to allow States to be sued in federal court," and that "to the extent that Parden v. Terminal Railway ... is inconsistent with the requirement that an abrogation of Eleventh

Amendment immunity by Congress must be expressed in unmistakably clear language, it is overruled." Id. at 475, 478, 107 S.Ct. at 2947, 2948.

[10][11][12][13] Although the Supreme Court overruled Parden's adoption of the doctrine of constructive consent, it is clear that it did so only to the extent that Parden allowed constructive consent to be found in the absence of unmistakably clear language expressing Congress' intent to subject the states to suit in federal court. Under Welch, a federal statute may still be used to waive a state's Eleventh Amendment immunity as long as: 1) Congress has indicated a clear and unmistakable intent to make the states liable in federal court if they engage in a particular activity; and 2) a state then voluntarily chooses to engage in that conduct. Id. See ERWIN CHEMERINSKY, FEDERAL JURISDICTION 410 (2d ed. 1994) (citing Pagan, Eleventh Amendment Analysis, 39 ARK.L.REV. 447, 494-95 (1986)). [FN12] Since "[c]onstructive consent is not a doctrine commonly associated ***218** with the surrender of constitutional rights," a constructive waiver of a state's Eleventh Amendment immunity may only be found where there exists an "unequivocal indication that the state intends to consent to federal jurisdiction that would otherwise be barred by the Eleventh Amendment." See Atascadero State Hosp., 473 U.S. at 238 n. 1, 105 S.Ct. at 3145 n. 1; Edelman, 415 U.S. at 673, 94 S.Ct. at 1360-61 (1974). In the current proceeding, therefore, the issue which must be decided is whether, in light of §§ 106(b) and (c) of the Bankruptcy Code, by counterclaiming, ICSAC has unequivocally and voluntarily acted to waive its constitutional right to immunity. [FN13]

FN12. Professor Chemerinsky states as follows:

In short, constructive waiver of Eleventh Amendment immunity is virtually nonexistent. If it ever will exist, it will be in situations where Congress indicates a clear intent to make states liable in federal court if they engage in a particular activity, and then a state voluntarily chooses to engage in that conduct. The congressional desire to make states liable must be in "unmistakable language in the statute itself" and it must be an area where the state realistically could choose not to engage in the activity.

CHEMERINSKY, supra, at 410. See also Gibson I, supra, at 346-47; S. Elizabeth Gibson, Sovereign Immunity in Bankruptcy: the Next Chapter, 70 AM.BANKR. L.J. 195, 211-12 (1996) [hereinafter Gibson II].

FN13. ICSAC argues that, to "resolve" the waiver issue, it will withdraw its counterclaim from this proceeding. This argument must fail, however, as it is antithetical to the definition of a waiver. Once a state waives its Eleventh Amendment immunity in a particular case, such action cannot ordinarily be undone. Cf. Hosp. Assoc. of N.Y. State, Inc. v. Toia, 435 F.Supp. 819, 827 (1977) (stating that a state should not ordinarily be permitted to waive its immunity from suit and then withdraw its consent).

ICSAC also argues that the filing of its Counterclaim in the current proceeding cannot possibly constitute a waiver because the Attorney General of Iowa does not possess the statutory authority under Iowa law to waive the state's sovereign immunity. It is true that, absent specific authorization by the state legislature, an Attorney General may not waive a state's Eleventh Amendment immunity by making a general appearance in federal court. Ford Motor Co. v. Dep't of Treasury, 323 U.S. 459, 467, 65 S.Ct. 347, 352, 89 L.Ed. 389 (1945); O'Connor v. Slaker, 22 F.2d 147, 152 (8th Cir.1927); Midland Mechanical Contractors, Inc., 200 B.R. at 458. In this case, however, the Attorney General did more than simply make a general appearance to defend on the merits. The Attorney General filed a counterclaim seeking affirmative relief in the form of a judgment. Iowa Code § 13.2(2) grants the Attorney General the authority to "[p]rosecute and defend in any other court or tribunal, all actions and proceedings, civil or criminal, in which the state may be a party or interested, when, in the attorney general's judgment, the interest of the state requires such action...." Iowa Code § 13.2(2) (1996). Section 13.2 thus authorizes the Attorney General to bring suit in federal court whenever the state's interests are at stake. See Iowa v. Scott & Fetzer Co., 1982 WL 1874, *2-3 (S.D.Iowa 1982). It follows from § 13.2 that, to the extent that such affirmative conduct constitutes a waiver under Eleventh Amendment law, the Attorney General is authorized to constructively waive Iowa's Eleventh Amendment immunity by bringing a claim in federal court. Therefore, although the Attorney General of Iowa does not possess the authority to waive Iowa's sovereign immunity by merely making a general appearance in federal court, this Court concludes that the Attorney General has the authority to waive Iowa's immunity by bringing a claim in federal court.

[14] Section 106(b) of the Bankruptcy Code

provides:

> A governmental unit that has filed a proof of claim in the case is deemed to have waived sovereign immunity with respect to a claim against such governmental unit that is property of the estate and arose out of the same transaction or occurrence out of which the claim of such governmental unit arose.

11 U.S.C. § 106(b) (1994). Section 106(c) provides:

> Notwithstanding any assertion of sovereign immunity by a governmental unit, there shall be offset against a claim or interest of the governmental unit any claim against such governmental unit that is property of the estate.

11 U.S.C. § 106(c) (1994). Plaintiff asserts that ICSAC's conduct in the face of §§ 106(b) and/or (c) constitutes a constructive waiver of its Eleventh Amendment immunity. Unlike the FELA in Parden or the Jones Act in Welch, subsections (b) and (c) of § 106 explicitly state Congress' intention to subject states to suit in federal court notwithstanding the Eleventh Amendment. Both subsections therefore satisfy the "unmistakable statutory language" standard set out in Welch. Nordic Village, 503 U.S. at 34, 112 S.Ct. at 1015.

Current § 106(b) specifically makes clear that, by filing a claim, a governmental unit waives its sovereign immunity as to any claim against it that is property of the estate [FN14] and that arose out of the same transaction *219 or occurrence out of which the governmental unit's claim arose. Section 106(b) therefore allows the estate to prevent the governmental unit from recovering on any claim it has against the estate as long as the claims arose out of the same transaction or occurrence. The constitutional underpinnings of § 106(b) are the many cases holding that, as a matter of law, a governmental unit that commences a case in federal court waives its sovereign immunity as to claims arising out of the same transaction or occurrence, at least up to the amount of its claim. See Gardner v. State of New Jersey, 329 U.S. 565, 67 S.Ct. 467, 91 L.Ed. 504 (1947); Clark v. Barnard, 108 U.S. at 436, 2 S.Ct. at 883; Genentech, Inc. v. Eli Lilly & Co., 998 F.2d 931, 946-47 (Fed.Cir.1993), cert. denied, Regents v. Genentech, Inc., 510 U.S. 1140, 114 S.Ct. 1126, 127 L.Ed.2d 434 (1994); U.S. v. Johnson, 853 F.2d 619, 621 (8th Cir.1988); Frederick v. U.S., 386 F.2d 481, 488 (5th Cir.1967); Fletcher v. U.S. Dep't of Energy, 763 F.Supp. 498, 502 (D.Kan.1991); Woelffer v. Happy States of America, Inc., 626 F.Supp. 499, 502 (N.D.Ill.1985); Bd. of Regents of the Univ. of Neb. v. Dawes, 370 F.Supp. 1190, 1191 (D.Neb.1974); Burgess v. M/V Tamano, 382 F.Supp. 351 (D.Me.1974), vacated on other grounds, 564 F.2d 964 (1st Cir.1977), cert. denied, M/V Tamano v. United States, 435 U.S. 941, 98 S.Ct. 1520, 55 L.Ed.2d 537 (1978). Unlike the recoupment cases, however, the waiver found in § 106(b) is unlimited in amount, and to this extent § 106(b) may be subject to constitutional challenge. Gibson I, supra, at 346-47; Gibson II, supra, at 210-11.

> FN14. Sections 106(b) and (c) each require the claim asserted against the governmental unit to be one that is property of the estate. Pursuant to 11 U.S.C. § 1306, the § 362(h) claim asserted in Count Two of the Plaintiff's Complaint constitutes property of the estate as "property ... that the debtor acquire[d] after the commencement of the case but before the case [was] closed, dismissed, or converted." United States v. McPeck (In re McPeck), 910 F.2d 509, 512 n. 7 (8th Cir.1990); Price v. United States (In re Price), 130 B.R. 259, 269 (N.D.Ill.1991); Flynn v. Internal Revenue Serv. (In re Flynn), 169 B.R. 1007, 1016 (Bankr.S.D.Ga.1994); In re Solis, 137 B.R. 121, 126 (Bankr.S.D.N.Y.1992).

Section 106(c)'s provision for waiver is much narrower than that provided in § 106(b). Section 106(c) merely provides that the estate may offset any claim it has against the governmental unit's claim or interest in the case, without regard to whether the estate's claim against the government arose out of the same transaction or occurrence as the government's claim. S.REP.NO. 95-989, at 29-30 (1978), reprinted in 1978 U.S.C.C.A.N. 5787, 5815-16; H.R.REP. NO. 95-595, at 317 (1977), reprinted in 1978 U.S.C.C.A.N. 5963, 6274. Unlike § 106(b), § 106(c) limits the amount of the estate's claim to the amount of the governmental unit's claim; it does not permit the estate to affirmatively recover against the governmental unit. Insofar as § 106(c) allows for the offset of claims which do not arise out of the same transaction or occurrence, however, it too may be subject to constitutional challenge. Gibson I, supra, at 346-47; Gibson II, supra, at 210-11.

The Court need not reach these constitutional

issues, however, since I conclude that neither § 106(b) nor § 106(c) apply to the facts of this case because ICSAC has not filed a proof of claim in the case.

Originally entitled §§ 106(a) and (b) respectively, current §§ 106(b) and (c) were both part of the 1978 Bankruptcy Code. As the legislative history to § 106 makes clear, current §§ 106(b) and (c) were originally intended to apply only in situations where a governmental unit has filed a proof of claim. S.REP. NO. 95-989, at 29-30 (1978), reprinted in 1978 U.S.C.C.A.N. 5787, 5815-16; H.R.REP. NO. 95-595, at 317 (1977), reprinted in 1978 U.S.C.C.A.N. 5963, 6274. The majority of the cases construing old § 106(a) and virtually all the cases construing old § 106(b) held that the filing of a claim by the governmental unit was a prerequisite to the application of either section. See Hoffman v. Conn. (In re Willington Convalescent Home Inc.), 850 F.2d 50 (2d Cir.1988); Neavear v. Schweiker (In re Neavear), 674 F.2d 1201 (7th Cir.1982); In re Husher, 131 B.R. 550 (E.D.N.Y.1991); Kincaid v. United States Veterans Admin. (In re Kincaid), 148 B.R. 844 (Bankr.E.D. Ky 1992); Hannan v. United States (In re Wilwerding), 130 B.R. 294 (Bankr.S.D.Iowa 1991); Saunders v. Reeher (In re Saunders), 105 B.R. 781, 789 (Bankr.E.D.Pa.1989); R.I. Ambulance Servs., Inc. v. Begin (In re R.I. Ambulance Servs., Inc.), 92 B.R. 4 (Bankr.D.R.I.1988); Inslaw, Inc. v. United States (In re Inslaw, Inc.), 76 B.R. 224, 229 n. 7 (Bankr.D.D.C.1987); In re Community Hosp. of Rockland County, 5 B.R. 7 (Bankr.S.D.N.Y.1979). When Congress *220 amended § 106 in 1994, it drastically modified old § 106(c) and renumbered it current § 106(a). Congress made only minor modifications to the wording of current §§ 106(b) and (c), however. [FN15] The Official Comments to the Bankruptcy Reform Act of 1994 indicate that the changes made to current § 106(b) were intended to clarify that the minority of cases which had held that old § 106(a) could apply even where the governmental unit had not filed a claim were incorrectly decided; [FN16] the Official Comments say nothing about the changes made in current § 106(c). 140 CONG.REC. H10,766 (daily ed. Oct. 4, 1994); Gibson I, supra, at 334- 37. [FN17] It appears, therefore, that the modifications made to current §§ 106(b) and (c) in 1994 did not change the fact that both subsections were originally and always meant to apply only where the governmental unit has filed a proof of claim. See Aetna Casualty & Surety Co. v. LTV Steel Co., Inc. (In re Chateaugay Corp.), 94 F.3d 772, 779 n. 10 (2d Cir.1996); Ossen v. Conn., 203 B.R. 17, 21-22 (Bankr.D.Conn.1996). But see 2 LAWRENCE P. KING ET AL., COLLIER ON BANKRUPTCY ¶ 106.03 (15th ed. 1996).

FN15. Section 106(b) now specifically requires the filing of a proof of claim by the governmental unit; § 106(c) was modified to delete the word "allowed" as a modifier of the word "claim."

FN16. The Official Comments to § 113 of the Bankruptcy Reform Act of 1994 read as follows:
Section 106(b) is clarified by allowing a compulsory counterclaim to be asserted against a governmental unit only where such unit has actively filed a proof of claim in the bankruptcy case. This has the effect of overruling contrary case law, such as Sullivan v. Town & Country Nursing Home [Home Nursing] Services, Inc., 963 F.2d 1146 (9th Cir.1992); In re Gribben, 158 B.R. 920 (S.D.N.Y.1993); and In re Craftsman [Craftsmen], Inc., 163 B.R. 88 (Bankr.W.D.Tex.1994), that interpreted § 106(a) of current law.
140 CONG.REC. H10,766 (daily ed. Oct. 4, 1994).

FN17. Remarks made by Senator Heflin just after the Senate passed § 106(c) indicate that redesignated § 106(c) was intended to codify existing § 106(b) and that no substantive changes were intended with regard to that section. See 140 CONG.REC. S 14,461 (daily ed. Oct. 6, 1994).

Because ICSAC has not filed a proof of claim in the Plaintiff's bankruptcy case, the requirements of §§ 106(b) and (c) have not been satisfied.

IV. RECOUPMENT

[15][16] The inapplicability of §§ 106(b) and 106(c), or of any other federal statute purporting to waive ICSAC's immunity from suit, does not end the Court's waiver inquiry, however. It has long been held that, when a state takes affirmative action to recover on a claim in federal court, the state waives its Eleventh Amendment immunity with respect to any counterclaims that arise out of the same transaction or occurrence as the state's claim; i.e., with respect to any compulsory counterclaims

asserted against the state. See Gardner, 329 U.S. at 573-74, 67 S.Ct. at 472; Genentech, Inc., 998 F.2d at 946-47; Jones v. Yorke (In re Friendship Med. Ctr, Ltd.), 710 F.2d 1297, 1300 (7th Cir.1983); Fletcher, 763 F.Supp. at 502; Woelffer, 626 F.Supp. at 502; Bd. of Regents of the Univ. of Neb., 370 F.Supp. at 1191; Burgess, 382 F.Supp. at 355. See generally 3 JAMES W. MOORE ET AL, MOORE'S FEDERAL PRACTICE, ¶ 13.19[2.-2] (2d ed. 1996). Cf. United States v. Forma, 42 F.3d 759, 764 (2d Cir.1994); Johnson, 853 F.2d at 621; Frederick, 386 F.2d at 488. Under this "recoupment theory" of waiver, the state's waiver is limited in scope to those counterclaims asserted for the purpose of defeating or diminishing the state's recovery, and no affirmative recovery against the state is permitted. Genentech, 998 F.2d at 947. The Supreme Court's recent Seminole decision contains no indication that the recoupment doctrine, a matter of long-standing immunity jurisprudence, has been undermined. See Employees, 411 U.S. at 295 n. 10, 93 S.Ct. at 1623 n. 10 (1973) (Marshall, J., concurring). See also Karen Cordry, Seminole, Sovereign Immunity, and the Supremacy Clause: The Sky Isn't Necessarily Falling, NORTON BANKRUPTCY LAW ADVISER, Dec. 1996, at 8.

[17][18] In this case, the filing of ICSAC's Counterclaim constitutes affirmative action, just as if ICSAC had filed a complaint. See Paul N. Howard v. P.R. Aqueduct Sewer Auth., 744 F.2d 880, 886 (1st Cir.1984) (holding that the filing of a counterclaim and third party complaint constitutes a waiver of a state's Eleventh Amendment immunity), *221 cert. denied, 469 U.S. 1191, 105 S.Ct. 965, 83 L.Ed.2d 970 (1985); Newfield House v. Mass. Dept. of Pub. Welfare, 651 F.2d 32, n. 3 (1st Cir.1981) (a state that sought removal to federal court and that filed a counterclaim waived its Eleventh Amendment immunity), cert. denied, 454 U.S. 1114, 102 S.Ct. 690, 70 L.Ed.2d 653 (1981); Cobb Coin Co., Inc. v. Unidentified, Wrecked & Abandoned Sailing Vessel, 549 F.Supp. 540, 555 (S.D.Fla.1982) (a state's intervention, filing of answer and counterclaim constitutes a waiver of sovereign immunity). Cf. Unix System Laboratories, Inc. v. Berkeley Software Design, Inc., 832 F.Supp. 790, 801 (D.N.J.1993) (stating that where a state is an affirmative participant in litigation it waives its defense of sovereign immunity). Unlike a mere general appearance by the state in federal court, the filing of a counterclaim constitutes affirmative conduct on the part of the state and is thus significantly more than a simple appearance in court for the purpose of defending on the merits or for the limited purpose of contesting jurisdiction. Cf. Mascheroni v. Board of Regents, 28 F.3d 1554, 1560 (10th Cir.1994). Therefore, the filing of ICSAC's Counterclaim in the current proceeding constitutes a waiver of its Eleventh Amendment immunity with respect to any claims asserted against it that arise out of the same transaction or occurrence upon which its Counterclaim is based.

[19] To determine whether competing claims "arise out of the same transaction or occurrence," courts have utilized the same analysis used to identify compulsory counterclaims under Federal Rule of Civil Procedure 13(a). Cochrane v. Iowa Beef Processors, Inc., 596 F.2d 254, 264 (8th Cir.1979), cert. denied, 442 U.S. 921, 99 S.Ct. 2848, 61 L.Ed.2d 290 (1979); Univ. Med. Ctr. v. Sullivan (In re Univ. Med. Ctr.), 973 F.2d 1065, 1086-87 (3d Cir.1992); United States v. Bulson (In re Bulson), 117 B.R. 537, 541 (9th Cir. BAP 1990), aff'd 974 F.2d 1341 (9th Cir.1992). See S.REP. NO. 95-989, at 29-30 (1978), reprinted in 1978 U.S.C.C.A.N. 5787, 5815. In the Eighth Circuit, the determination of whether competing claims "arise out of the same transaction or occurrence," is made by considering one or more of the following four factors:

(1) Are the issues of fact and law raised by the claim and counterclaim largely the same?
(2) Would res judicata bar a subsequent suit on defendant's claim absent the compulsory counterclaim rule?
(3) Will substantially the same evidence support or refute plaintiff's claim as well as defendant's counterclaim?
(4) Is there any logical relation between the claim and the counterclaim?

Cochrane, 596 F.2d at 264. In United States v. McPeck, 910 F.2d 509, 512 (8th Cir.1990), the Court of Appeals for the Eighth Circuit specifically refrained from deciding the question of whether a debtor's claim for damages for violation of the automatic stay arises out of the same transaction or occurrence as a governmental unit's claim for recovery of the underlying debt. In the case of Tullos v. Parks, 915 F.2d 1192, 1195 (8th Cir.1990), however, the Eighth Circuit emphasized the importance of the logical relation test in making

this determination, stating that "the logical relation test provides the needed flexibility for applying Rule 13(a)."

[20] Applying the logical relation test to the facts of this case, this Court agrees with the clear majority of available case law and concludes that a debtor's § 362(h) claim against a governmental unit is logically related to the governmental unit's claim for recovery of the underlying debt. See, e.g., Price v. United States (In re Price), 42 F.3d 1068, 1074 (7th Cir.1994); Univ. Med. Ctr., 973 F.2d at 1086-87; Bulson, 117 B.R. at 541; United States v. Lile (In re Lile), 161 B.R. 788, 791 (S.D.Tex.1993); United States v. Fernandez (In re Fernandez), 132 B.R. 775, 780 (M.D.Fla.1991); Flynn v. Internal Revenue Serv. (Matter of Flynn), 169 B.R. 1007, 1017 (Bankr.S.D.Ga.1994). Accordingly, this Court holds that the Plaintiff's § 362(h) claim against ICSAC arises out of the same transaction or occurrence as ICSAC's claim for recovery of the underlying debt. In so holding, the Court is mindful of Rule 13(a)'s goal of preventing a multiplicity of actions and a duplication of judicial efforts, as well as the general deterrent policies underlying § 362(h) of the Bankruptcy Code. Therefore, *222 by choosing to file a counterclaim in this case, ICSAC has waived its Eleventh Amendment immunity from suit as to Count Two of the Plaintiff's Complaint to the extent that the Plaintiff's damages under Count Two are equal to or less than ICSAC's Counterclaim for judgment in the amount of the underlying debt. Cf. Langenkamp v. Culp, 498 U.S. 42, 44, 111 S.Ct. 330, 331, 112 L.Ed.2d 343 (1990); In re Lazar, 200 B.R. at 380-81.

ACCORDINGLY, IT IS HEREBY ORDERED THAT Defendant ICSAC's Motion to Dismiss is DENIED.

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In the Matter of MERCHANTS GRAIN, INCORPORATED, Debtor.
Appeal of Edmund M. MAHERN, Trustee for Merchants Grain, Incorporated.

No. 94-1721.

United States Court of Appeals, Seventh Circuit.

Argued Sept. 19, 1994.

Decided June 30, 1995.

Chapter 11 trustee initiated adversary proceeding against Ohio Agricultural Commodity Depositors Fund and Ohio Commodity Advisory Commission, seeking to recover alleged preferential transfers made for benefit of Fund to Ohio farmers. The United States Bankruptcy Court for the Southern District of Indiana dismissed proceeding, and appeal was taken. The District Court, McKinney, J., affirmed, and trustee appealed. The Court of Appeals, Grant, District Judge, sitting by designation, held that: (1) state of Ohio was real party in interest, and, thus, Eleventh Amendment would bar proceeding, absent waiver by state or valid congressional override; (2) Congress had authority to abrogate Eleventh Amendment when it acted pursuant to powers accorded it under bankruptcy clause; and (3) Congress did not act arbitrarily and irrationally in giving retroactive application to Bankruptcy Reform Act's sovereign immunity waiver.

Reversed and remanded.

[1] BANKRUPTCY ⚿2679
51k2679
State of Ohio was real party in interest in Chapter 11 trustee's adversary proceeding against Ohio Agricultural Commodity Depositors Fund and Ohio Commodity Advisory Commission, seeking to recover alleged preferential transfers made for benefit of Fund to Ohio farmers, and, therefore, Eleventh Amendment would bar adversary proceeding absent waiver by State or valid congressional override, where, under plain language of Ohio statutes, any judgment rendered against Fund or Commission would effectively be judgment against state. U.S.C.A. Const.Amend. 11; Ohio R.C. §§ 926.16(A, D), 926.18(A, C, D), 926.19(C), 926.32(A, B, G-I), 926.33(B).

[1] BANKRUPTCY ⚿2723
51k2723
State of Ohio was real party in interest in Chapter 11 trustee's adversary proceeding against Ohio Agricultural Commodity Depositors Fund and Ohio Commodity Advisory Commission, seeking to recover alleged preferential transfers made for benefit of Fund to Ohio farmers, and, therefore, Eleventh Amendment would bar adversary proceeding absent waiver by State or valid congressional override, where, under plain language of Ohio statutes, any judgment rendered against Fund or Commission would effectively be judgment against state. U.S.C.A. Const.Amend. 11; Ohio R.C. §§ 926.16(A, D), 926.18(A, C, D), 926.19(C), 926.32(A, B, G-I), 926.33(B).

[2] FEDERAL COURTS ⚿269
170Bk269
Where state-created entity gets money to pay its debts, including any judgments which may be entered against it, is relevant to Eleventh Amendment inquiry if nature of entity in question is unclear. U.S.C.A. Const.Amend. 11.

[3] BANKRUPTCY ⚿2679
51k2679
Congress had authority under bankruptcy clause to abrogate state's Eleventh Amendment immunity pursuant to provisions of Bankruptcy Code. U.S.C.A. Const. Art. 1, § 8, cl. 4; Amend. 11; Bankr.Code, 11 U.S.C.A. § 106(a).

[4] COURTS ⚿89
106k89
It is holding of Supreme Court, not identities of justices joining in it, that creates stare decisis.

[5] FEDERAL COURTS ⚿265
170Bk265
Congress has authority to abrogate states' immunity from suit when legislating pursuant to plenary powers granted it under Article I. U.S.C.A. Const. Art. 1, § 1; Amend. 11.

[6] BANKRUPTCY ⚿2023

51k2023
Burden was on Ohio Agricultural Commodity Depositors Fund and Ohio Commodity Advisory Commission, as parties asserting constitutional violation arising out of retroactivity of Bankruptcy Reform Act's waiver of sovereign immunity, to establish that Congress acted in arbitrary and irrational manner. U.S.C.A. Const.Amend. 11; Bankr.Code, 11 U.S.C.A. § 106(a).

[6] BANKRUPTCY ⚖2679
51k2679
Burden was on Ohio Agricultural Commodity Depositors Fund and Ohio Commodity Advisory Commission, as parties asserting constitutional violation arising out of retroactivity of Bankruptcy Reform Act's waiver of sovereign immunity, to establish that Congress acted in arbitrary and irrational manner. U.S.C.A. Const.Amend. 11; Bankr.Code, 11 U.S.C.A. § 106(a).

[6] CONSTITUTIONAL LAW ⚖48(4.1)
92k48(4.1)
Burden was on Ohio Agricultural Commodity Depositors Fund and Ohio Commodity Advisory Commission, as parties asserting constitutional violation arising out of retroactivity of Bankruptcy Reform Act's waiver of sovereign immunity, to establish that Congress acted in arbitrary and irrational manner. U.S.C.A. Const.Amend. 11; Bankr.Code, 11 U.S.C.A. § 106(a).

[7] BANKRUPTCY ⚖2023
51k2023
Ohio Agricultural Commodity Depositors Fund and Ohio Commodity Advisory Commission did not establish that Congress acted in arbitrary and irrational manner in making Bankruptcy Reform Act's sovereign immunity provision retroactive to pending cases, since Congress had always intended to have comprehensive waiver of sovereign immunity under Bankruptcy Code and wanted Bankruptcy Reform Act to clarify that point once and for all. Bankr.Code, 11 U.S.C.A. § 106.

[7] BANKRUPTCY ⚖2679
51k2679
Ohio Agricultural Commodity Depositors Fund and Ohio Commodity Advisory Commission did not establish that Congress acted in arbitrary and irrational manner in making Bankruptcy Reform Act's sovereign immunity provision retroactive to pending cases, since Congress had always intended to have comprehensive waiver of sovereign immunity under Bankruptcy Code and wanted Bankruptcy Reform Act to clarify that point once and for all. Bankr.Code, 11 U.S.C.A. § 106.

*631 Joseph H. Yeager, Jr., James M. Carr, Wendy W. Ponader (argued), Baker & Daniels, Indianapolis, IN, for Edmund M. Mahern.

William B. Logan, Jr. (argued), Kenneth M. Richards, Luper, Wolinetz, Sheriff & Neidenthal, Columbus, OH, Cheryl Minsterman, Ohio Dept. of Agriculture, Reynoldsburg, OH, for Ohio Agricultural Commodity Depositors Fund, Ohio Commodity Advisory Com'n.

James M. Carr, Baker & Daniels, Indianapolis, IN, for Merchants Grain, Inc.

Before BAUER and MANION, Circuit Judges, and GRANT, District Judge. [FN*]

FN* The Honorable Robert A. Grant of the United States District Court for the Northern District of Indiana is sitting by designation.

GRANT, District Judge.

Edmund Mahern, as Trustee for Merchants Grain, Inc. (hereinafter "MGI"), initiated an adversary proceeding in the bankruptcy court against the defendants, the Ohio Agricultural Commodity Depositors Fund and the Ohio Commodity Advisory Commission, seeking to recover alleged preferential transfers made for the benefit of the Fund in the 90 days preceding the filing of MGI's bankruptcy petition under 11 U.S.C. §§ 547 and 550. The defendants asserted an Eleventh Amendment defense, and the bankruptcy court dismissed the proceeding. The district court affirmed, and this appeal followed. For the following reasons, we now REVERSE and REMAND.

I. Factual Background

The Ohio Agricultural Commodity Depositors Fund was created by the Ohio legislature to indemnify grain depositors (primarily farmers) who lose money due to the insolvency of commodity handlers licensed by the State of Ohio. The money in the Fund comes from a per-bushel fee paid by the depositors to licensed commodity handlers, who in

turn remit the money to the Fund. Pursuant to statute, the Fund is a part of the state treasury, and is administered by the Director of the Department of Agriculture. The Ohio Commodity Advisory Commission was established to aid the Director in his duties with respect to the Fund.

During 1990, MGI operated grain elevators and held commodity handlers licenses in Ohio and several other states. In the fall of 1990, MGI purchased large quantities of grain and other commodities at all of its facilities, including its elevator in Columbus, Ohio. MGI bought much of this grain under deferred pricing contracts, taking title to the grain without paying for it or immediately setting a *632 price. The farmers became unsecured creditors of MGI for the purchase price of the grain, with the right to set that price and collect their money weeks or months later.

On November 8, 1990, the Ohio Department of Agriculture, fearing that MGI was insolvent, conditionally suspended its license. The Department directed MGI to liquidate all grain stored at its Columbus, Ohio facility to cover MGI's obligations to Ohio farmers under its deferred payment contracts.

As a result of the Department's intervention, Ohio farmers were paid over $3 million on antecedent debts within the 90 days preceding MGI's Chapter 11 petition, money which otherwise would have been paid out of the Fund. Although virtually all Ohio "delayed pricing" depositors were paid as a result of this action, over 700 farmers in three other states, including Indiana, were left with unpaid claims exceeding $19 million.

MGI filed its Chapter 11 petition in bankruptcy on May 9, 1991, and Edmund Mahern was appointed trustee on March 24, 1992. On March 12, 1992, Mr. Mahern initiated an adversary proceeding under 11 U.S.C. §§ 547(b) and 550(a)(1) to recover the preferential transfers made for the benefit of the Fund to Ohio farmers in an amount exceeding $2.7 million. The defendants filed a motion to dismiss, contending that they were immune from suit for monetary damages under the Eleventh Amendment. The bankruptcy court agreed and granted the defendants' motion.

II. The Eleventh Amendment

A. The Defendants' Relationship to the State

[1] At the time oral arguments were heard, the sole issue on appeal was whether the Fund and the Commission were "the State of Ohio" for Eleventh Amendment purposes.

The Trustee contends that the key factor in determining whether a state- created entity is "the State" for Eleventh Amendment purposes has always been the source of funds from which its debts and judgments are paid. He maintains that where, as here, the source of funding does not come from the general revenues of the State, the entity is not an "arm of the State" and, therefore, is not immune from suit.

The bankruptcy court concluded, however, that the real party in interest in this case was clearly the State of Ohio, and that the source of funds from which the recovery would come was, therefore, irrelevant. Paschal v. Jackson, 936 F.2d 940, 944 (7th Cir.1991), cert. denied, 502 U.S. 1081, 112 S.Ct. 992, 117 L.Ed.2d 152 (1992). We agree.

[2] Where a state-created entity gets the money to pay its debts, including any judgments which may be entered against it, is relevant to an Eleventh Amendment inquiry if the nature of the entity in question is unclear. See Hess v. Port Authority Trans-Hudson Corp., --- U.S. ----, ---- - ----, 115 S.Ct. 394, 402-406, 130 L.Ed.2d 245 (1994); Mercer v. Magnant, 40 F.3d 893, 898-99 (7th Cir.1994); Paschal, 936 F.2d at 944. There can be no doubt in the present case, however, that the State of Ohio is the real party in interest.

Under Ohio law, the Fund is a part of the state treasury, O.S.C. § 926.16(A), and is administered by the Director of the Ohio Department of Agriculture (a state official acting in his official capacity and compensated by the State). O.S.C. § 926.16(D); Emerson v. Seville Elevator Co., 38 Ohio App.3d 55, 526 N.E.2d 95, 95 (1987). All claims for indemnification from the Fund are filed with the Director, who assesses the validity of the claim and provides for payment. O.S.C. §§ 926.18(A) and (C). Pursuant to § 926.18(D), "all disbursements from the [F]und shall be paid by the treasurer of state pursuant to vouchers authorized by the Director." Commission members are appointed by the Director of Agriculture, and serve only in an

advisory capacity. O.S.C. § 926.32(A). The Director designates who serves as chairman of the Commission, and may, after notice and public hearing, remove any member for neglect of duty or malfeasance in office. O.S.C. § 926.32(B). The Director provides the meeting space, assistance, services, and data necessary to enable the Commission to carry out its functions. O.S.C. § 926.32(G). The Director also designates "an official or employee of the department *633 of agriculture to act as the executive secretary of the commission." O.S.C. § 926.32(I). All costs of the Commission, including all of the expenses of its members and consultants, are paid from the commodity handler regulatory program fund created in section 926.19 pursuant to itemized vouchers which must be approved by the Director. O.S.C. § 926.32(H). O.S.C. § 926.19(C) expressly provides that: "If at any time the moneys deposited in the [regulatory program] fund ... are not sufficient to pay the examination and administrative costs of this chapter, the director shall request an appropriation from the general revenue fund to pay those costs." (Emphasis added).

The relationship between the defendants and the State of Ohio is further clarified in § 926.33(B), which provides:

> This chapter is enacted for the benefit of the state, and neither the state, its departments, agencies, or commissions, or its employees and officials either elected or appointed, shall be held liable for any injuries to third parties, for the exercise of their authority, or for the use of their discretion on the matters to which this chapter relates.

Section 926.33 thus evidences a clear intent to bring the Fund and the Commission within the protections accorded the State under the doctrine of sovereign immunity. As the bankruptcy court aptly noted: "The state treasurer and the Director, sued in his or her official capacity, and the Department of Agriculture would no doubt be considered 'the state' for Eleventh Amendment purposes (which is probably why none were named as a party)." See Mercer, 40 F.3d at 899 ("a state official sued in an official capacity ... is treated as a 'state' "); Allinder v. State of Ohio, 808 F.2d 1180, 1184 (6th Cir.1987) (Ohio Department of Agriculture and Director of Department, when sued in his official capacity, are the "State" for purposes of asserting Eleventh Amendment immunity).

Given the plain language of the Ohio statutes, any judgment rendered against the Fund or the Commission would effectively be a judgment against the State of Ohio. "Where the state gets the money to pay [that] judgment ... is irrelevant ..." Mercer, 40 F.3d at 899 (citing Alabama v. Pugh, 438 U.S. 781, 98 S.Ct. 3057, 57 L.Ed.2d 1114 (1978)); Paschal, 936 F.2d at 944.

B. Abrogation of Immunity Under 11 U.S.C. § 106

"[A]bsent waiver by the State or valid congressional override," the Eleventh Amendment would have barred the Trustee's action against the Fund and the Commission, Kentucky v. Graham, 473 U.S. 159, 169, 105 S.Ct. 3099, 3107, 87 L.Ed.2d 114 (1985). The Bankruptcy Code, however, contained a waiver provision at the time the defendants' filed their motion. 11 U.S.C. § 106 provided that:

> (a) A governmental unit is deemed to have waived sovereign immunity with respect to any claim against such governmental unit that is property of the estate and that arose out of the same transaction or occurrence out of which such governmental unit's claim arose.
> (b) There shall be offset against an allowed claim or interest of a governmental unit any claim against such governmental unit that is property of the estate.
> (c) Except as provided in subsections (a) and (b) of this section and notwithstanding any assertion of sovereign immunity--
> (1) a provision of this title that contains "creditor", "entity", or "governmental unit" applies to governmental units; and
> (2) a determination by the court of an issue arising under such a provision binds governmental units.

While subsections (a) and (b) unequivocally provided for a waiver of immunity when the "governmental unit" had filed a proof of claim and thereby consented to being sued, United States v. Nordic Village, Inc., 503 U.S. 30, 34, 112 S.Ct. 1011, 1014-1015, 117 L.Ed.2d 181 (1992); Hoffman v. Connecticut Dept. of Income Maintenance, 492 U.S. 96, 101-102, 109 S.Ct. 2818, 2822-2823, 106 L.Ed.2d 76 (1989); In re Price, 42 F.3d 1068, 1070 (7th Cir.1994); In re Midway Airlines, Inc., 175 B.R. 239, 244 (Bankr.N.D.Ill.1994), there was no indication in the present case that the State of Ohio had ever filed a claim against the bankruptcy estate. Which left

*634 subsection (c) as the Trustee's only line of defense.

In In re McVey Trucking, 812 F.2d 311, 326-327 (7th Cir.), cert. denied, 484 U.S. 895, 108 S.Ct. 227, 98 L.Ed.2d 186 (1987), we held that § 106(c) clearly applied to preference avoidance actions initiated against a governmental unit under § 547(b), and unequivocally waived the government's right to assert sovereign immunity as a bar to the proceeding. When the issue came before the Supreme Court two years later, however, the Court took a different viewpoint, and held that § 106(c) did not contain the express and unequivocal language required to effectively abrogate the Eleventh Amendment immunity of the States. Hoffman, 492 U.S. at 100-104, 109 S.Ct. at 2822- 2824. See also Nordic Village, 503 U.S. at 33-37, 112 S.Ct. at 1014-1016.

Citing Nordic Village and Hoffman as controlling authority, the bankruptcy court held that, absent the State's consent, the Eleventh Amendment barred the Trustee's action to recover the preferential transfers. While that was a correct statement of the law at the time the bankruptcy court issued its decision, the law has since changed.

On October 22, 1994, a month after oral arguments had been completed in this case, the Bankruptcy Reform Act of 1994, Pub.L. No. 103-394, 108 Stat. 4106 (1994), was enacted. One of the key changes effected was the amendment of § 106.

Pursuant to section 113 of the Reform Act, 11 U.S.C. § 106(c) was amended and recodified as § 106(a), and provides:

> Waiver of sovereign immunity
>
> (a) Notwithstanding an assertion of sovereign immunity, sovereign immunity is abrogated as to a governmental unit to the extent set forth in this section with respect to the following:
>
> (1) Sections 105, 106, 107, 108, 303, 346, 362, 363, 364, 365, 366, 502, 503, 506, 510, 522, 523, 524, 525, 542, 543, 544, 545, 546, 547, 548, 549, 550, 551, 552, 553, 722, 724, 726, 728, 744, 749, 764, 901, 922, 926, 928, 929, 944, 1107, 1141, 1142, 1143, 1146, 1201, 1203, 1205, 1206, 1227, 1231, 1301, 1303, 1305, and 1327 of this title....

(Emphasis added). 11 U.S.C. § 106(a) (as amended Pub.L. 103-394, Title I, § 113, Oct. 22, 1994, 108 Stat. 4117). The amendment was intended to effectively overrule Nordic Village and Hoffman, and to "clarify[ ] the original intent of Congress in enacting Section 106 of the Bankruptcy Code with regard to sovereign immunity." 140 Cong.Rec. H10752-01, H10772 and H10766. Congress accordingly provided that § 113 was to be applied retroactively to bankruptcy cases which were "commenced before ... the date of the enactment". Pub.L. 103-394, § 702(b)(2)(B) of the Reform Act (set out as a note under 11 U.S.C. § 101).

[3] The defendants do not dispute the fact that the abrogation language in § 106(a) as amended is express and unequivocal, but rather contend that the abrogation provision is invalid because Congress has no authority under the Bankruptcy Clause, Art. I, § 8, cl. 4, to abrogate the States' Eleventh Amendment immunity. According to the defendants, Congress can override the Eleventh Amendment only when it acts pursuant to § 5 of the Fourteenth Amendment. Defendants contend, in the alternative, that even if Congress has the power, it cannot exercise it retroactively. We disagree.

That Congress can abrogate the States' Eleventh Amendment immunity when it acts pursuant to the plenary powers accorded it under § 5 of the Fourteenth Amendment is not disputed. See Dellmuth v. Muth, 491 U.S. 223, 227, 109 S.Ct. 2397, 2400, 105 L.Ed.2d 181 (1989); Atascadero State Hospital v. Scanlon, 473 U.S. 234, 238, 105 S.Ct. 3142, 3145, 87 L.Ed.2d 171 (1985); Fitzpatrick v. Bitzer, 427 U.S. 445, 456, 96 S.Ct. 2666, 2671, 49 L.Ed.2d 614 (1976). The question before us is whether it may also do so under its Article I plenary powers. We held that it can in McVey Trucking, concluding that there was no constitutional basis for distinguishing between the plenary powers accorded Congress under the Fourteenth Amendment and those accorded under Article I. McVey Trucking, 812 F.2d at 316-323. Accord United States v. Union Gas Co., 832 F.2d 1343, 1352 (3d Cir.1987), aff'd, 491 U.S. *635 1, 109 S.Ct. 2273, 105 L.Ed.2d 1 (1989); County of Monroe v. Florida, 678 F.2d 1124 (2d Cir.1982), cert. denied, 459 U.S. 1104, 103 S.Ct. 726, 74 L.Ed.2d 951 (1983); Peel v. Florida Dept. of Transportation, 600 F.2d 1070, 1080-81 (5th Cir.1979); Mills Music, Inc. v. Arizona, 591 F.2d 1278 (9th Cir.1979). The Supreme Court reached the same conclusion in Pennsylvania v. Union Gas Co., 491 U.S. 1, 109 S.Ct. 2273, 105 L.Ed.2d 1

(1989).

Justice Brennan, who authored the plurality opinion in which Justices Marshall, Blackmun, and Stevens joined, concluded that:

> Like the Fourteenth Amendment, the Commerce Clause with one hand gives power to Congress while, with the other, it takes power away from the States ... that is the meaning, in fact, of a "plenary" grant of authority, and the lower courts have rightly concluded that it makes no sense to conceive of § 5 [of the Fourteenth Amendment] as somehow being an "ultraplenary" grant of authority. See, e.g., In re McVey Trucking, supra, at 316.

Union Gas, 491 U.S. at 16-17, 109 S.Ct. at 2283. Justice White cast the fifth and decisive vote, concluding that Congress did indeed have the authority under Article I to abrogate the States' Eleventh Amendment immunity. Union Gas, 491 U.S. at 57, 109 S.Ct. at 2296 (White, J. concurring).

The defendants are quick to point out, however, that there was a vehement dissent in Union Gas. Justice Scalia, who authored the dissent on behalf of Chief Justice Rehnquist and Justices O'Connor and Kennedy, would hold that state immunity from suit in federal courts is a "structural component of federalism" that Congress cannot alter by legislation enacted pursuant to its Article I powers. Union Gas, 491 U.S. at 29-45, 109 S.Ct. at 2289-2290 (Scalia, J., dissenting, joined by Rehnquist, C.J., and O'Connor and Kennedy, JJ.). See also Hoffman, 492 U.S. at 105, 109 S.Ct. at 2824-2825 (Scalia and O'Connor, JJ., concurring). The dissent reasoned that:

> [I]f the Article I commerce power enables abrogation of state sovereign immunity, so do all the other Article I powers. An interpretation of the original Constitution which permits Congress to eliminate sovereign immunity only if it wants to renders the doctrine a practical nullity and is therefore unreasonable. The Fourteenth Amendment, on the other hand, was avowedly directed against the power of the States, and permits abrogation of their sovereign immunity only for a limited purpose.

Union Gas, 491 U.S. at 42, 109 S.Ct. at 2303.

The defendants contend that Union Gas was wrongly decided and should not be considered controlling authority in this case. They note that the composition of the Court has changed significantly since the decision was handed down, with the majority losing two key votes, and surmise that it is only a matter of time before the dissent's viewpoint becomes the law of the land and Union Gas is overturned. The defendants accordingly urge us to adopt what they perceive to be the law of the future. We must decline the invitation.

[4][5] As the First Circuit noted in Reopell v. Commonwealth of Massachusetts, 936 F.2d 12, 15-16 (1st Cir.), cert. denied, 502 U.S. 1004, 112 S.Ct. 637, 116 L.Ed.2d 655 (1991): "The battle may not yet be ended, but we are constrained to accept the Court's majority pronouncements." See also In re York-Hannover Developments, Inc., 181 B.R. 271 (Bankr.E.D.N.C.1995). It is the Court's holding, not the identities of the justices joining in it, that creates stare decisis. See Payne v. Tennessee, 501 U.S. 808, 844-845, 851-855, 111 S.Ct. 2597, 2619, 2622-2623, 115 L.Ed.2d 720 (1991) (Marshall, J., and Blackmun, J., dissenting).

> When a fragmented Court decides a case and no single rationale explaining the result enjoys the assent of five Justices, "the holding of the Court may be viewed as that position taken by those Members who concurred in the judgments on the narrowest grounds...."

Marks v. United States, 430 U.S. 188, 193, 97 S.Ct. 990, 993, 51 L.Ed.2d 260 (1977) (quoting Gregg v. Georgia, 428 U.S. 153, 169 n. 15, 96 S.Ct. 2909, 2923 n. 15, 49 L.Ed.2d 859 (1976) (opinion of Stewart, Powell, and Stevens, JJ.)). It should thus come as no surprise *636 that virtually every Court of Appeals to have reached the issue since Union Gas has concluded that Congress has the authority to abrogate the States' immunity from suit when legislating pursuant to the plenary powers granted it under Article I of the Constitution. See, e.g., Ponca Tribe of Oklahoma v. State of Oklahoma, 37 F.3d 1422, 1429-30 (10th Cir.1994), petition for cert. filed, 63 U.S.L.W. 3477 (Dec. 9, 1994); Brinkman v. Dept. of Corrections of the State of Kansas, 21 F.3d 370, 371-72 (10th Cir.), cert. denied, 513 U.S. 927, 115 S.Ct. 315, 130 L.Ed.2d 277 (1994); Reich v. State of New York, 3 F.3d 581, 590 (2d Cir.1993), cert. denied, 510 U.S. 1163, 114 S.Ct. 1187, 127 L.Ed.2d 537 (1994); Hale v. State of Arizona, 993 F.2d 1387, 1391 (9th Cir.), cert. denied, 510 U.S. 946, 114 S.Ct. 386, 126 L.Ed.2d 335 (1993); State of New York v.

United States, 942 F.2d 114, 121 (2d Cir.1991), aff'd in part and rev'd in part, 505 U.S. 144, 112 S.Ct. 2408, 120 L.Ed.2d 120 (1992); Reopell, 936 F.2d at 15-16. [FN1] We find no basis for holding otherwise today.

> FN1. But see Seminole Tribe of Florida v. State of Florida, 11 F.3d 1016, 1023 (11th Cir.1994) (recognizing that Congress has specifically abrogated the Eleventh Amendment defense when legislating pursuant to § 5 of the Fourteenth Amendment and its Article I, § 8 plenary power over commerce, but refusing to extend authority to abrogate to legislation enacted pursuant to the Indian Commerce Clause (the Indian Gaming Regulatory Act)).

The defendants' perfunctory challenge to the retroactive application of § 113 deserves little comment. The Fund and Commission contend that they would be unduly prejudiced if the amendment were to be applied retroactively to their case because it would allow the Trustee to pursue a cause of action which otherwise would have been barred by the applicable statute of limitations. They are incorrect.

The issue before the court is not whether the change in the law effected by the Reform Act would allow the Trustee to bring a new adversary proceeding against the defendants, but whether it precluded dismissal of the old one. If the retroactive application of § 113 is constitutional, and we must presume that it is, Pension Benefit Guaranty Corp. v. R.A. Gray & Co., 467 U.S. 717, 729, 104 S.Ct. 2709, 2717-2718, 81 L.Ed.2d 601 (1984); Usery v. Turner Elkhorn Mining Co., 428 U.S. 1, 15-26, 96 S.Ct. 2882, 2892-2897, 49 L.Ed.2d 752 (1976), the judgment of dismissal must be reversed. [FN2] Plaut v. Spendthrift Farm, Inc., 514 U.S. 211, ----, 115 S.Ct. 1447, 1457, 131 L.Ed.2d 328 (1995) (when Congress has expressly provided that a new law is to be applied retroactively we "must apply that law in reviewing judgments still on appeal that were rendered before the law was enacted, and must alter the outcome accordingly"). See also United States v. Schooner Peggy, 5 U.S. (1 Cranch) 103, 109, 2 L.Ed. 49 (1801); Landgraf v. USI Film Products, 511 U.S. 244, ---- - ----, 114 S.Ct. 1483, 1500-1508, 128 L.Ed.2d 229 (1994); Carpenter v. Wabash R. Co., 309 U.S. 23, 60 S.Ct. 416, 84 L.Ed. 558 (1940) (amendment to Bankruptcy Act effected while case was pending on petition for writ of certiorari given effect where amendment expressly provided for retroactive application); In re Anton Motors, Inc., 177 B.R. 58 (Bankr.D.Md.1995) (section 106 as amended by the Bankruptcy Reform Act of 1994 applicable where bankruptcy case commenced before the statute's enactment, and even though statute of limitations for initiating adversary proceedings expired before the change in the law was effected); but see In re Bison Heating & Equipment, Inc., 177 B.R. 785 (Bankr.W.D.N.Y.1995).

> FN2. To the extent 11 U.S.C. § 106(a) could be read to require federal courts to reopen final judgments entered before the Reform Act was enacted, it may indeed be subject to a constitutional challenge, see Spendthrift Farm, 514 U.S. 211, ---- - ----, 115 S.Ct. 1447, 1451-1463, 131 L.Ed.2d 328 (1995). That is not the case before us, however, as the judgment of the Bankruptcy Court is not yet final.

[6][7] "A challenged statute is constitutional so long as its retroactive application--like any future application--is justified by a 'legitimate legislative purpose furthered by rational means.' " Long Island Oil Products Co., Inc. v. Local 553 Pension Fund, 775 F.2d 24, 27 (2d Cir.1985) (quoting Pension Benefit Guaranty, 467 U.S. at 729, 104 S.Ct. at 2717-2718). The burden is on the defendants in this case, as the parties asserting a *637 constitutional violation, to establish that Congress acted in an arbitrary and irrational manner. See Turner Elkhorn Mining Co., 428 U.S. at 15, 96 S.Ct. at 2892. The defendants' unfounded allegations of prejudice fall far short of the mark.

Defendants do not dispute the fact that the retroactive application of § 113 furthers a legitimate legislative purpose, nor could they. Section 113 was applied retroactively for a very simple reason: Congress had always intended 11 U.S.C. § 106 to be a comprehensive waiver of sovereign immunity and wanted to clarify that point once and for all. 140 Cong.Rec. H10752-01, H10772 and H10766. In doing so, Congress effectively advanced the general purpose of the bankruptcy system by "enforcing a distribution of the debtor's assets in an orderly manner in which the claims of all creditors are considered fairly, in accordance with established principles rather than on the basis of the inside influence or economic leverage of a particular creditor." H.R.REP. 103-835. State and Federal

governments "must abide by the regular processes of the bankruptcy court applicable to all claimants." 140 Cong.Rec. H10752-01, H10772.

III. Conclusion

We conclude on the basis of the foregoing discussion that Congress has the authority to abrogate the Eleventh Amendment when it acts pursuant to the powers accorded it under the Bankruptcy Clause, Art. I, § 8, cl. 4; that it expressly and unequivocally did so when it enacted § 113 of the Reform Act, 11 U.S.C. § 106; and that § 113 applies retroactively to this case. Accordingly, the judgment is REVERSED and the cause REMANDED.

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In re Juan Ortiz MARTINEZ and Ellyha Torres, Debtors.

Civil No. 92-1925 (JP).
Bankruptcy No. 85-01691 (ESL).

United States District Court, D. Puerto Rico.

May 15, 1996.

Chapter 13 debtors sought monetary judgment against Department of Treasury of the Commonwealth of Puerto Rico for alleged willful violation of automatic stay, due to postpetition filing of tax lien on debtors' property. The Bankruptcy Court denied relief. Debtors appealed. The District Court, Pieras, J., held that: (1) Treasury had not filed proof of claim in debtors' bankruptcy case, and thus it did not waive its right of sovereign immunity under Bankruptcy Code, and (2) to extent Bankruptcy Code sovereign immunity provision purports to apply to governmental units of state and Commonwealth governments, it is unconstitutional violation of states' right to sovereign immunity under Eleventh Amendment.

Affirmed.

[1] BANKRUPTCY ⇦2786
51k2786
Bankruptcy Court's findings of fact shall be upheld unless they are clearly erroneous, while its conclusions of law are reviewed de novo.

[1] BANKRUPTCY ⇦3782
51k3782
Bankruptcy Court's findings of fact shall be upheld unless they are clearly erroneous, while its conclusions of law are reviewed de novo.

[2] BANKRUPTCY ⇦2402(4)
51k2402(4)
Department of Treasury of the Commonwealth of Puerto Rico violated automatic stay when Treasury filed tax lien over debtors' property after Chapter 13 petition had been filed. Bankr.Code, 11 U.S.C.A. § 362.

[3] BANKRUPTCY ⇦2391
51k2391
Automatic stay gives "breathing spell" to debtor and stops all collection efforts, all harassment, and all foreclosure actions. Bankr.Code, 11 U.S.C.A. § 362.

[4] BANKRUPTCY ⇦2679
51k2679
Department of Treasury of the Commonwealth of Puerto Rico had not filed proof of claim in Chapter 13 debtors' bankruptcy case, and thus Treasury did not waive its right of sovereign immunity under Bankruptcy Code, and it was not amenable to suit for monetary damages for willful violation of automatic stay, based on its filing of tax lien against debtors' property. U.S.C.A. Const.Amend. 11; Bankr.Code, 11 U.S.C.A. §§ 106, 362.

[5] FEDERAL COURTS ⇦265
170Bk265
Object and purpose of Eleventh Amendment were to prevent indignity of subjecting State to coercive process of judicial tribunals at instance of private parties. U.S.C.A. Const.Amend. 11.

[6] FEDERAL COURTS ⇦268.1
170Bk268.1
For purposes of Eleventh Amendment sovereign immunity analysis, Commonwealth of Puerto Rico is treated as a State. U.S.C.A. Const.Amend. 11.

[7] FEDERAL COURTS ⇦265
170Bk265
Scope of Eleventh Amendment protection extends to government of state itself, and to "arms" of the state. U.S.C.A. Const.Amend. 11.

[8] FEDERAL COURTS ⇦5
170Bk5
Federal courts are courts of limited jurisdiction, and as such are authorized to do only those things provided by Constitution and federal law.

[9] FEDERAL COURTS ⇦265
170Bk265
Eleventh Amendment limits scope of subject matter jurisdiction of federal courts, granted to federal courts by Article 3, § 2 of the United States Constitution, by withdrawing from federal court's jurisdiction any case between state and citizens of

another state. U.S.C.A. Const. Art. 3, § 2, cl. 2; Amend. 11.

[9] FEDERAL COURTS ⚿268.1
170Bk268.1
Eleventh Amendment limits scope of subject matter jurisdiction of federal courts, granted to federal courts by Article 3, § 2 of the United States Constitution, by withdrawing from federal court's jurisdiction any case between state and citizens of another state. U.S.C.A. Const. Art. 3, § 2, cl. 2; Amend. 11.

[10] FEDERAL COURTS ⚿265
170Bk265
Federal court may exercise jurisdiction over case between state and citizen of another state, if state waives its claim of immunity or if Congress abrogates states' claim of immunity. U.S.C.A. Const.Amend. 11.

[10] FEDERAL COURTS ⚿268.1
170Bk268.1
Federal court may exercise jurisdiction over case between state and citizen of another state, if state waives its claim of immunity or if Congress abrogates states' claim of immunity. U.S.C.A. Const.Amend. 11.

[11] FEDERAL COURTS ⚿265
170Bk265
In determining whether Congress has abrogated States' sovereign immunity so as to subject States to suit in federal court, courts ask first whether Congress has unequivocally expressed its intent to abrogate immunity, and second whether Congress has acted pursuant to valid exercise of power. U.S.C.A. Const.Amend. 11.

[11] FEDERAL COURTS ⚿268.1
170Bk268.1
In determining whether Congress has abrogated States' sovereign immunity so as to subject States to suit in federal court, courts ask first whether Congress has unequivocally expressed its intent to abrogate immunity, and second whether Congress has acted pursuant to valid exercise of power. U.S.C.A. Const.Amend. 11.

[12] BANKRUPTCY ⚿2679
51k2679
Governmental unit must file proof of claim in bankruptcy case before bankruptcy court may deem that governmental unit waived its right to sovereign immunity. U.S.C.A. Const.Amend. 11; Bankr.Code, 11 U.S.C.A. §§ 106, 362.

[13] BANKRUPTCY ⚿2679
51k2679
To extent Bankruptcy Code sovereign immunity provision purports to apply to governmental units of State and Commonwealth governments, it is unconstitutional violation of States' right to sovereign immunity under Eleventh Amendment. U.S.C.A. Const. Art. 1, § 8, cl. 3; Amend. 11; Bankr.Code, 11 U.S.C.A. § 106.

[13] FEDERAL COURTS ⚿265
170Bk265
To extent Bankruptcy Code sovereign immunity provision purports to apply to governmental units of State and Commonwealth governments, it is unconstitutional violation of States' right to sovereign immunity under Eleventh Amendment. U.S.C.A. Const. Art. 1, § 8, cl. 3; Amend. 11; Bankr.Code, 11 U.S.C.A. § 106.

[13] FEDERAL COURTS ⚿268.1
170Bk268.1
To extent Bankruptcy Code sovereign immunity provision purports to apply to governmental units of State and Commonwealth governments, it is unconstitutional violation of States' right to sovereign immunity under Eleventh Amendment. U.S.C.A. Const. Art. 1, § 8, cl. 3; Amend. 11; Bankr.Code, 11 U.S.C.A. § 106.

[14] FEDERAL COURTS ⚿265
170Bk265
Eleventh Amendment restricts judicial power under Article III, and Article I cannot be used to circumvent constitutional limitations placed upon federal jurisdiction. U.S.C.A. Const. Art. 1, § 8, cl. 3; Amend. 11.

***226** Irving K. Hernandez, Rio Piedras, PR, for Appellant.

Viviana Rodriguez Ortiz, Hato Rey, PR, for Appellee Treasury Dept. of the Commonwealth of Puerto Rico.

OPINION AND ORDER

PIERAS, District Judge.

The Court has before it an appeal pursuant to 28 U.S.C. § 158(a) from the Opinion and Order of the Bankruptcy Court, dated January 17, 1992, denying debtors' request for the imposition of a monetary judgment for willful violation of the automatic stay against the Department of Treasury of the Commonwealth of Puerto Rico (hereinafter referred to as "Treasury"). The issue before the Court is whether Treasury waived its sovereign immunity such that the Bankruptcy Court had jurisdiction over the arm of the government. The Bankruptcy Court determined that Treasury had not filed a proof of claim in debtors' case, therefore Treasury had not waived its sovereign immunity under section 106(a) of the Bankruptcy Code. Consequently, the Bankruptcy Court determined that it had no jurisdiction to find Treasury liable for actual monetary damages for a willful violation of the bankruptcy stay. After carefully reviewing the record and the arguments presented, the Bankruptcy Court's decision is hereby AFFIRMED.

I. SUMMARY OF STIPULATED FACTS

On November 22, 1985, debtors Juan Ortiz Martinez and Ellyha Torres filed a voluntary petition for bankruptcy relief under Chapter 13 of the Bankruptcy Code. On April 23, 1986, a reorganization plan was confirmed by the Bankruptcy Court. Debtors had listed a debt to the Department of the Treasury of the Commonwealth of Puerto Rico in the amount of $16,000.00 in their schedule of creditors and debts. Nonetheless, Treasury never filed a proof of claim in the bankruptcy proceedings.

On December 15, 1989, Treasury filed a tax lien over debtors real property in the local, Puerto Rico property Registrar, and thereafter notified debtors of the lien. Treasury originally calculated its lien as covering the years of 1975 to 1987, in the amount of $102,951.42, divided as follows: approximately $58,754.98 in pre-petition income tax from 1975-1984; approximately $33,511.37 in post-petition income tax from 1985-1989. Treasury subsequently clarified that these *227 amounts had incorrectly included amounts for a time period which was precluded by the statute of limitations. Treasury corrected the erroneous notification as follows: approximately $21,179.83 in pre-petition income tax from 1982 to 1984; approximately $36,701.09 in post-petition income tax from 1985 to 1987; the tax incurred from 1975-1981 had prescribed. Finally, Treasury asserted that none of these amounts were subject to discharge because Treasury asserted that it had been improperly notified of the debtors' petition. Therefore, Treasury asserted that the final amount of its lien over debtor's property was for a corrected total of $57,880.92.

On May 17, 1991, debtors filed an application for an order to show cause as to why actual and punitive damages should not be assessed against Treasury for willful violation of the automatic stay, due to the post-petition filing of the tax lien on debtors' property. On July 23, 1991, the Bankruptcy Court held a hearing to consider debtors' motions, and thereafter allowed the parties forty- five days to address two questions: 1) whether this proceeding should be filed as an adversary proceeding, and 2) whether the Bankruptcy Court could assess damages against an instrumentality of the government of the Commonwealth of Puerto Rico. Moreover, the Bankruptcy Court made findings of fact that Treasury was aware that debtors had filed a voluntary petition in bankruptcy because it had received a copy of the petition, even if the petition did not include Mr. Juan Manuel Ortiz's social security number, and because debtors had visited Treasury in an attempt to notify Treasury of the bankruptcy petition.

On January 17, 1992, the Bankruptcy Court issued the Opinion and Order which is the subject of this appeal. The Bankruptcy Court held that Treasury had not filed a proof of claim against debtors' estate, therefore, Treasury had not waived its right of sovereign immunity under 11 U.S.C. § 106(a). Moreover, the Bankruptcy Court determined that it lacked the authority to impose a monetary sanction against an instrumentality of the government of the Commonwealth of Puerto Rico, pursuant to 11 U.S.C. § 106(c). Finally, the Court refused to determine the validity of Treasury's lien over debtor's property, finding that this issue should be determined in an adversary proceeding, pursuant to Rule 7001(2) of the Bankruptcy Rules. On February 7, 1992, debtors filed their first notice of appeal which was designated Civil Case No. 92-1596 (JP). Simultaneous with the notice of appeal, debtors filed a motion for reconsideration with the Bankruptcy Court. This Court dismissed debtors' first appeal in Civil Case No. 92-1596 (JP), because it had been

filed prior to the Bankruptcy Court's decision of the debtor's motion for reconsideration, and therefore the notice of appeal was invalid pursuant to Rule 8002(b) of the Bankruptcy Rules.

Upon considering debtors' motion for reconsideration, the Bankruptcy Court made additional findings of fact, granted the motion, and held that Treasury had violated the automatic stay of 11 U.S.C. § 362(a). Therefore, the Court awarded debtors attorneys' fees of $1,000.00 plus costs.

Immediately thereafter, Treasury filed a motion for reconsideration, which the Bankruptcy Court denied on May 28, 1992. Also on May 28, 1992, the debtors filed their second notice of appeal, appealing the Bankruptcy Court's original Order denying the imposition of monetary damages against Treasury for willful violation of the automatic stay.

II. STANDARD OF REVIEW

[1] The Bankruptcy Court's findings of fact shall be upheld unless they are clearly erroneous, and the Bankruptcy Court's conclusions of law, shall be reviewed de novo. T I Fed. Credit Union v. DelBonis, 72 F.3d 921, 928 (1st Cir.1995).

III. DISCUSSION

The issue on appeal is whether the Department of Treasury of the Commonwealth of Puerto Rico had waived its Eleventh Amendment right of sovereign immunity, such that the Bankruptcy Court would have jurisdiction over debtors' claim that Treasury had willfully violated the automatic stay.

*228 A. AUTOMATIC STAY

[2] Debtors contend that Treasury willfully violated the automatic stay by placing a lien on the debtors' property, and therefore is liable for monetary damages to debtors. Debtors further contend that Treasury waived any claim to sovereign immunity even though it never filed a proof of claim in the debtors' Chapter 13 bankruptcy case.

[3] The moment that a debtor files a petition in bankruptcy, creditors of the debtor estate are prevented from taking any act to obtain possession of the estate property, to create a lien against the estate property, or to collect, assess, or recover a claim against a debtor that arose before the commencement of the debtor's bankruptcy case. 11 U.S.C. § 362(a)(3),(4) and (6). This provision of the Bankruptcy Code, referred to as the automatic stay, "gives a 'breathing spell' to the debtor and stops 'all collection efforts, all harassment, and all foreclosure actions.' " Tringali v. Hathaway Machinery Co., Inc., 796 F.2d 553, 562 (1st Cir.1986) (citing legislative history). For this reason, the stay has been referred to as an "essential foundation block of the bankruptcy rebuilding process," In re Patterson, 125 B.R. 40, 47 (Bankr.N.D.Ala.1990). In fact, "Congress intended that the automatic stay be 'one of the fundamental debtor protections provided by the bankruptcy laws,' " In re Solis, 137 B.R. 121, 124 (Bankr.S.D.N.Y.1992) (citing legislative history).

The Bankruptcy Code provides for remedies of the violation of the automatic stay:

> 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. 11 U.S.C. § 362(h).

In the case at bar, it is clear that Treasury violated the debtors' automatic stay when Treasury filed a tax lien over debtors' property after the Chapter 13 petition had been filed. Debtors contend that this violation of the stay was willful because Treasury had actual knowledge that debtors had filed their bankruptcy petition at the time that Treasury registered its lien on debtors' property. Therefore, debtors requested that the Bankruptcy Court permit debtors to recover actual damages, costs and attorneys' fees from Treasury.

B. WAIVER OF SOVEREIGN IMMUNITY

[4][5][6][7] Treasury contends that it has not waived its right to sovereign immunity protected by the Eleventh Amendment, therefore, the Bankruptcy Court does not have jurisdiction to contemplate debtors' request for the imposition of a monetary judgment against Treasury. The Eleventh Amendment provides:

> The Judicial power of the United States shall not be construed to extend to any suit in law or equity, commenced or prosecuted against one of the United States by Citizens of another State, or by Citizens or Subjects of any Foreign State.

" 'The very object and purpose of the 11th

Amendment were to prevent the indignity of subjecting a State to the coercive process of judicial tribunals at the instance of private parties,' " Puerto Rico Aqueduct & Sewer Authority v. Metcalf & Eddy, 506 U.S. 139, 146, 113 S.Ct. 684, 688-89, 121 L.Ed.2d 605 (1993) (citing In re Ayers, 123 U.S. 443, 8 S.Ct. 164, 31 L.Ed. 216 (1887)). For the purposes of Eleventh Amendment sovereign immunity analysis, the Commonwealth of Puerto Rico is treated as a State. Ramirez v. Puerto Rico Fire Serv., 715 F.2d 694, 697 (1st Cir.1983); In re San Juan Dupont Plaza Hotel Fire Litigation, 888 F.2d 940, 942 (1st Cir.1989); De Leon Lopez v. Corporacion Insular de Seguros, 931 F.2d 116, 121 (1st Cir.1991). The scope of the Eleventh Amendment protection extends to the government of the state itself, and to "arms" of the state, Metcalf & Eddy v. Puerto Rico Aqueduct & Sewer Authority, 991 F.2d 935, 939 (1st Cir.1993). There is no dispute in the case at bar that Treasury is entitled to Eleventh Amendment sovereign immunity.

[8][9] It is a fundamental tenet of federal jurisdiction that federal courts are courts of limited jurisdiction, and as such are "authorized to do only those things provided by the Constitution and federal law." In re York- Hannover Developments, Inc., 190 B.R. 62, *229 65 (Bankr.E.D.N.C.1995). The Eleventh Amendment limits the scope of subject matter jurisdiction of federal courts, granted to federal courts by Section 2 of Article III of the United States Constitution, by withdrawing from the federal court's jurisdiction any case between a state and citizens of another state. Id. at 64.

[10] Nonetheless, a federal court may exercise jurisdiction over a case between a state and a citizen of another state, if either the state waives its claim of immunity or if Congress abrogates the states' claim of immunity. Pennhurst State School & Hosp. v. Halderman, 465 U.S. 89, 99, 104 S.Ct. 900, 907-08, 79 L.Ed.2d 67 (1984).

[11] "In order to determine whether Congress has abrogated the States' sovereign immunity, we ask two questions: first, whether Congress has 'unequivocally expresse[d] its intent to abrogate the immunity,' and second, whether Congress has acted 'pursuant to a valid exercise of power,' " Seminole Tribe of Florida v. Florida, --- U.S. ----, ----, 116 S.Ct. 1114, 1123, 134 L.Ed.2d 252 (1996) (citing Green v. Mansour, 474 U.S. 64, 68, 106 S.Ct. 423, 88 L.Ed.2d 371 (1985)).

[12] In the case at bar, at the time that the parties filed their briefs, the Bankruptcy Code specifically provided that:

> A governmental unit is deemed to have waived sovereign immunity with respect to any claim against such governmental unit that is property of the estate and that arose out of which such governmental unit's claim arose. 11 U.S.C. § 106(a).

The Bankruptcy Code defines a "government unit" as United States; States; Commonwealth; District; Territory; .... or instrumentality of the United States ... Commonwealth, 11 U.S.C. § 101(27). Therefore, this provision purports to provide for the waiver of sovereign immunity of both the federal and state government.

At the time that appellant filed this appeal, there existed confusion among the courts, however, concerning whether a governmental unit could have been deemed to have waived its right to sovereign immunity under § 106(a), if the governmental unit had not filed a proof of claim in the debtors' bankruptcy case. The Supreme Court has stated in obiter dicta that the filing of a claim will waive sovereign immunity under § 106(a) and suggests that the filing of a claim is necessary for finding a strict waiver: "Neither § 106(a) nor § 106(b) provides a basis for petitioner's actions here, since respondents did not file a claim in either Chapter 7 proceeding," Hoffman v. Conn. Dept. of Income Maintenance, 492 U.S. 96, 101, 109 S.Ct. 2818, 2822-23, 106 L.Ed.2d 76 (1989).

Nevertheless, several courts rejected this dicta of the Supreme Court, and relied instead upon an interpretation of the plain terms of the statutory provisions to hold that the filing of a proof of claim was not a prerequisite. See In re Craftsmen, 163 B.R. 88 (Bankr.N.D.Tex., 1993) ("the filing of a proof of claim does not serve as a prerequisite to a waiver of sovereign immunity pursuant to § 106(a)); In re Operation Open City, 170 B.R. 818 (S.D.N.Y.1994); In re T.F. Stone Companies, Inc., 170 B.R. 884 (Bankr.N.D.Tex.1994). In Matter of Washington, 172 B.R. 415 (Bankr.S.D.Ga.1994) ("All that is necessary is that the governmental unit possess a claim, not that it assert it in any fashion"); In re Boldman, 148 B.R. 874 (Bankr.C.D.Ill.1993).

On October 22, 1994, Congress amended § 106(a) under the Bankruptcy Reform Act of 1994, Publ.L. No. 103-394, 108 Stat. 4106 (1994) to read as follows:

> A governmental unit that has filed a proof of claim in the case is deemed to have waived sovereign immunity with respect to a claim against such governmental unit that is property of the estate and that arose out of the same transaction or occurrence out of which the claim of such governmental unit arose. (Emphasis added). 11 U.S.C. § 106(b).

Congress specifically provided that the amendments to § 106 apply retroactively. **Matter of Merchants Grain, Inc., 59 F.3d 630, 634 (7th Cir.**1995), cert. granted and judgment vacated, Ohio Agricultural Commodity v. Mahern, --- U.S. ----, 116 S.Ct. 1411, 134 L.Ed.2d 537 (1996). Therefore, Congress unequivocally requires that the ***230** governmental unit file a proof of claim in the bankruptcy case before the bankruptcy court may deem that the governmental unit waived its right to sovereign immunity. This clarification effectively overruled prior case law holding that the filing of a proof of claim was not necessary. In re HPA Associates, 191 B.R. 167, 171-72 (9th Cir. BAP 1995). Thus, after the 1994 amendment, Congress made an "unmistakenly clear" statutory statement abrogating States' right to sovereign immunity, if the governmental unit filed a proof of claim.

Based upon the facts of the case, Treasury did not file a proof of claim in debtors' bankruptcy case. Therefore, according to the statutory provision, Treasury did not waive its claim to sovereign immunity, and it is not amenable to suit for willful violation of the stay. Although the issue as presented by the parties in the case at bar is hereby disposed, it is important to take note of the effect of a recent decision from the Supreme Court of the United States of America, and to analyze the effect of this decision on the issue in the case at bar.

[13] The second stage of the inquiry into congressional abrogation of Eleventh Amendment analysis requires the Court to determine whether Congress' unequivocal statement purporting to abrogate state sovereign immunity was taken pursuant to a valid exercise of Congressional power. The Supreme Court has recently held that Congress does not have constitutional authority to abrogate the States' Eleventh Amendment right to sovereign immunity, pursuant to the Bankruptcy Clause. Ohio Agricultural Commodity v. Mahern, --- U.S. ----, 116 S.Ct. 1411. The Supreme Court did not analyze the question of Congressional authority specifically as it applies to the Bankruptcy Clause, Article I, clause 8. It merely remanded based upon its decision that Congress does not have authority under the Indian Commerce Clause, Article I, Section 8, clause 3, to abrogate the States' Eleventh Amendment protection of sovereign immunity. Seminole, --- U.S. ----, 116 S.Ct. 1114, 134 L.Ed.2d 252 (1996).

Prior to this recent decision of the Supreme Court, the majority of courts which had analyzed this issue, held that Congress may abrogate the States' Eleventh Amendment immunity pursuant to its legislating authority accorded by Article I's Bankruptcy Clause, which reads:

> "[t]he Congress shall have the power ... [t]o establish ... uniform Laws on the subject of Bankruptcies through the United States." Article I, clause 8.

See **In re Merchants Grain, Inc., 59 F.3d 630, 636 (7th Cir.**1995); In re McVey Trucking, Inc., 812 F.2d 311 (7th Cir.), cert. denied sub nom. Edgar v. McVey Trucking Inc., 484 U.S. 895, 108 S.Ct. 227, 98 L.Ed.2d 186 (1987).

[14] The Supreme Court, however, has clearly stated that the prior analysis is erroneous. "The Eleventh Amendment restricts the judicial power under Article III, and Article I cannot be used to circumvent the constitutional limitations placed upon federal jurisdiction." Seminole, --- U.S. at ---- - ----, 116 S.Ct. at 1131-32. Therefore, the Supreme Court specifically found § 106 of the Bankruptcy Code, as it purports to apply to governmental units of State and Commonwealth governments, an unconstitutional violation of States' right to sovereign immunity protected by the Eleventh Amendment.

IV. CONCLUSION

Treasury has not voluntarily waived its claim of sovereign immunity and consented to be sued in federal court by debtors for violation of the stay. Therefore, the Bankruptcy Court lacks jurisdiction over debtors claim against Treasury for willful violation of the automatic stay. Consequently, the Opinion and Order dated January 12, 1992, finding

In the Matter of Julian E. FERNANDEZ, Debtor.

Civ.A. No. 97-0083.

United States District Court, E.D. Louisiana.

April 16, 1997.

ORDER AND REASONS

CARR, District Judge.

*1 The State of Louisiana, Department of Transportation and Development, appeals a bankruptcy court decision. The State was made a defendant in an adversary action involving property which the State purchased from the debtor, and moved for dismissal on Eleventh Amendment immunity. The bankruptcy court denied dismissal and entered judgment against the State and others.

The primary issue is whether Congress, acting under the bankruptcy clause of Article I of the Constitution, may abrogate the sovereign immunity of the States, as reflected in the Eleventh Amendment, and subject States to federal court jurisdiction.

In denying the motion to dismiss, the bankruptcy court relied on 11 U.S.C. § 106(a) of the Bankruptcy Code, [FN1] which was intended to abrogate the State's sovereign immunity, and on **Matter of Merchants Grain, Inc., 59 F.3d 630 (7th Cir.**1995), vacated and remanded, --- U.S. ----, 116 S.Ct. 1411, 134 L.Ed.2d 537 (1996), which found that § 106(a) was a valid exercise of Congress' Article I powers to abrogate that immunity. **Merchants Grain** in turn depended on Pennsylvania v. Union Gas Co., 491 U.S. 1, 109 S.Ct. 2273, 105 L.Ed.2d 1 (1989), in which the Court found that the powers of Congress under Article I included the power to abrogate the States' immunity. After the bankruptcy court's action, the Supreme Court in Seminole Tribe of Florida v. Florida, --- U.S. ----, 116 S.Ct. 1114, 134 L.Ed.2d 252 (1996), overruled Union Gas, thus negating the analysis of **Merchants Grain**, on which the bankruptcy court had relied. [FN2]

FN1. Which provides, in part:
Notwithstanding an assertion of sovereign immunity, sovereign immunity is abrogated as to a governmental unit to the extent set forth in this section with respect to [certain sections of the code, including the section at issue in the adversary proceeding].

FN2. **Merchants Grain** was remanded for reconsideration "in light of Seminole Tribe."

Seminole Tribe involved the Article I Indian Commerce Clause and the intent of Congress in the Indian Gaming Regulatory Act, 25 U.S.C. § 2701, et seq., to abrogate the States' immunity by providing that tribes could sue States in federal court. The Supreme Court held that the Article I powers of Congress do not extend to abrogation of the Eleventh Amendment. The Court's opinion refers broadly to Article I, concluding:

> Even when the Constitution vests in Congress complete law-making authority over a particular area, the Eleventh Amendment prevents congressional authorization of suits by private parties against unconsenting states. The Eleventh Amendment restricts the judicial power under Article III, and Article I cannot be used to circumvent the constitutional limitations placed upon federal jurisdiction.

--- U.S. ----, 116 S.Ct. 1131-1132.

After Seminole Tribe, it is clear that though Article I "vests in Congress complete lawmaking authority" as to bankruptcy, § 106(a), enacted pursuant to Article I, cannot be a valid abrogation of the States' sovereign immunity.

The only constitutional authority by which Congress may abrogate Eleventh Amendment immunity is § 5 of the Fourteenth Amendment. Seminole Tribe, supra. That section provides Congress the "power to enforce, by appropriate legislation, the provisions" of that Amendment. A law is "appropriate legislation" to enforce the Amendment if, in part, it "may be regarded" as an enactment to enforce the Amendment. Katzenbach v. Morgan, 384 U.S. 641, 651, 86 S.Ct. 1717, 1724, 16 L.Ed.2d 828 (1966). [FN3]

FN3. Congress need not specify that a law is enacted pursuant to the Fourteenth Amendment in order to abrogate sovereign immunity under § 5. Equal Employment Opportunity Commission v. Wyoming, 460 U.S. 226, 243 n. 18, 103 S.Ct. 1954, 1064 n. 18 (1983).

*2 Section 106(a) of the Bankruptcy Code may not be regarded as an enactment to enforce the Fourteenth Amendment. The cases in which abrogation of sovereign immunity has been upheld under § 5 involve unlawful discrimination by state actors. See Wilson-Jones v. Caviness, 99 F.3d 203 (6th Cir.1996). Discrimination is not an issue in § 106.

IT IS ORDERED that the judgment of the bankruptcy court against the State of Louisiana, Department of Transportation and Development, is REVERSED; and that the State of Louisiana, Department of Transportation and development, is DISMISSED from this action. The Clerk of Court is directed to certify the fact of the questioning of the constitutionality of 11 U.S.C. § 106(a) to the Attorney General. 28 U.S.C. § 2403.

END OF DOCUMENT

In re Ronald TAIBBI, d/b/a Satin & Lace Photography Studios, a/k/a Ronald M. Taibbi, a/k/a Ronnie Taibbi, a/k/a Ron Taibbi, a/k/a Ronald Tiabbi, a/k/a Ron Tiabbi and Patricia Taibbi, d/b/a Satin & Lace Photography Studios, a/k/a Patricia A. Taibbi, a/k/a Patricia Taivvi, a/k/a Patricia Tiabbi, a/k/a Pat Tiabbi, Debtors.

Bankruptcy No. 095-71313-511.

United States Bankruptcy Court, E.D. New York.

Sept. 25, 1997.

County consumer protection agency, which had fined Chapter 7 debtors $10,500 for engaging in deceptive trade practices in connection with their wedding photography business, moved for order granting it extension of time to file adversary complaint objecting to debtors' discharge or to determine dischargeability of debts, including those debts owed to individual consumers. The Bankruptcy Court, Melanie L. Cyganowski, J., held that: (1) agency had statutory standing to commence adversary proceeding on behalf of consumer creditors; (2) agency had standing to commence adversary proceeding under doctrine of parens patriae; (3) agency established "cause" to extend its time to file complaint; and (4) absent filing of adversary proceeding, court could not issue judicial declaration that debt owed to agency was nondischargeable as fine or civil penalty payable to governmental unit.

Motion granted.

[1] BANKRUPTCY ⚿2825
51k2825
When enacting the Bankruptcy Code, Congress intended to adopt broadest possible definition of "claim." Bankr.Code, 11 U.S.C.A. § 101(5).
See publication Words and Phrases for other judicial constructions and definitions.

[2] BANKRUPTCY ⚿2825
51k2825
For purposes of the Bankruptcy Code, meanings of terms "debt" and "claim" are coextensive. Bankr.Code, 11 U.S.C.A. § 101(5, 12).
See publication Words and Phrases for other judicial constructions and definitions.

[3] BANKRUPTCY ⚿2825
51k2825
For purposes of Bankruptcy Code provision defining "claim" as right to payment, phrase "right to payment" means nothing more or less than an enforceable obligation. Bankr.Code, 11 U.S.C.A. § 101(5).
See publication Words and Phrases for other judicial constructions and definitions.

[4] ACTION ⚿3
13k3
To determine whether private right of action exists where none is expressed in statute, courts apply three-part test, assessing whether plaintiff is one of the class for whose particular benefit statute was enacted, whether recognition of private right of action would promote legislative purpose, and whether creation of such right would be consistent with legislative scheme.

[5] BANKRUPTCY ⚿3385
51k3385
County consumer protection agency had statutory standing to commence adversary proceeding against Chapter 7 debtors to determine dischargeability of debts owed to consumer creditors; local consumer protection law authorized agency to seek restitution and to sue to enforce restitution stipulation, which gave agency right to payment or "enforceable obligation" on behalf of injured consumers, and public policy also favored standing. Bankr.Code, 11 U.S.C.A. § 523(c)(1); Suffolk County Code §§ 249, 17-1992.

[6] STATES ⚿190
360k190
"Parens patriae," or "parent of the country," which refers traditionally to role of state as sovereign and guardian of persons under legal disability and embodies principle that state must care for those who cannot take care of themselves, is used, as doctrine of standing, to protect government's quasi-sovereign interests, such as interest in health and well-being of its residents in general.
See publication Words and Phrases for other judicial constructions and definitions.

[7] STATES ⚿190

360k190
To have standing under doctrine of parens patriae, governmental entity must establish that state has quasi-sovereign interest, apart from interests of particular private parties, that there is injury to substantial segment of state's population, and that individuals could not obtain complete relief through private lawsuit.

[8] BANKRUPTCY ⚿3385
51k3385
County consumer protection agency had standing, under doctrine of parens patriae, to commence adversary proceeding against Chapter 7 debtors to determine dischargeability of debts owed to consumer creditors; county had quasi-sovereign interest, apart from its residents, in ensuring that consumers within its borders were protected from unfair or deceptive business practices, agency had received 64 consumer complaints against debtors in connection with their wedding photography business, it was not clear that consumers could have brought action under county consumer protection law, which did not appear to create private right of action and, even if they could have brought private actions, amounts of individual debts may have been too small to warrant engagement of counsel to file adversary complaints. Suffolk County Code § 249.

[9] BANKRUPTCY ⚿3312
51k3312
County consumer protection agency established "cause" to extend its time to file adversary complaint objecting to Chapter 7 debtors' discharge or to determine dischargeability of debts where agency needed additional time to investigate some 60 consumer complaints against debtors, most of which were filed within month or two of petition date and some of which were dated postpetition. Bankr.Code, 11 U.S.C.A. §§ 523, 727.

[9] BANKRUPTCY ⚿3383
51k3383
County consumer protection agency established "cause" to extend its time to file adversary complaint objecting to Chapter 7 debtors' discharge or to determine dischargeability of debts where agency needed additional time to investigate some 60 consumer complaints against debtors, most of which were filed within month or two of petition date and some of which were dated postpetition. Bankr.Code, 11 U.S.C.A. §§ 523, 727.

[10] BANKRUPTCY ⚿3382.1
51k3382.1
If creditor has any ground to except debt from discharge under subsections governing false pretenses or actual fraud, fraud or defalcation, willful and malicious injury, or nonsupport divorce debt, creditor must file timely adversary complaint or forever lose his or her rights; creditor holding other grounds to except debt from discharge, however, need not file complaint within 60 days, and his or her failure to do so will not result in automatic discharge of debt. Bankr.Code, 11 U.S.C.A. § 523(a)(2, 4, 6, 15), (c)(1); Fed.Rules Bankr.Proc.Rule 4007(c), 11 U.S.C.A.

[11] BANKRUPTCY ⚿2060.1
51k2060.1
Bankruptcy court has exclusive jurisdiction to determine dischargeability of debts under subsections governing false pretenses or actual fraud, fraud or defalcation, willful and malicious injury, and nonsupport divorce debt, but concurrent jurisdiction with respect to debts falling within other paragraphs of discharge exceptions statute. Bankr.Code, 11 U.S.C.A. § 523(a)(2, 4, 6, 15).

[12] BANKRUPTCY ⚿2060.1
51k2060.1
Dischargeability of debts under paragraphs of discharge exceptions statute other than subsections governing false pretenses or actual fraud, fraud or defalcation, willful and malicious injury, and nonsupport divorce debt may be determined at any time, in any forum. Bankr.Code, 11 U.S.C.A. § 523(a)(2, 4, 6, 15).

[12] BANKRUPTCY ⚿3382.1
51k3382.1
Dischargeability of debts under paragraphs of discharge exceptions statute other than subsections governing false pretenses or actual fraud, fraud or defalcation, willful and malicious injury, and nonsupport divorce debt may be determined at any time, in any forum. Bankr.Code, 11 U.S.C.A. § 523(a)(2, 4, 6, 15).

[13] BANKRUPTCY ⚿3358
51k3358
Absent filing of adversary proceeding, bankruptcy court could not issue judicial declaration that debt owed to agency by Chapter 7 debtors was

nondischargeable as fine or civil penalty payable to governmental unit. Bankr.Code, 11 U.S.C.A. § 523(a)(7).

[13] BANKRUPTCY ⚿3381
51k3381
Absent filing of adversary proceeding, bankruptcy court could not issue judicial declaration that debt owed to agency by Chapter 7 debtors was nondischargeable as fine or civil penalty payable to governmental unit. Bankr.Code, 11 U.S.C.A. § 523(a)(7).

***263** Stanley Somer & Associates by Jeffrey T. Heller, Commack, NY, for Debtors.

Robert J. Cimino, Suffolk County Attorney by Janice A. Whelan, Assistant County Attorney, Hauppauge, NY, for Suffolk County Executive Office of Citizens Affairs.

OPINION and ORDER

MELANIE L. CYGANOWSKI, Bankruptcy Judge.

The Suffolk County Executive's Office of Citizen Affairs ("OCA") [FN1] is the agency chosen by Suffolk County to investigate instances of fraud allegedly practiced upon the consumers within its borders. In April of 1995, OCA issued 21 notices of violation of the Suffolk County Consumer Protection Law to Ronald and Patricia Taibbi, d/b/a Satin and Lace Photography Studios (the "Debtors"), alleging deceptive trade practices in that the Debtors failed to deliver wedding photographs and/or issue refunds as promised in contracts executed with prospective brides and grooms. Rather than defend that proceeding, the Debtors filed--45 minutes prior to the hearing scheduled by an OCA hearing officer--a voluntary petition seeking relief under chapter 7, listing on their schedules 289 individual creditors holding claims arising from such contracts which aggregate slightly more than $637,000. [FN2]

FN1. OCA is an administrative agency created by the Suffolk County Legislature in Local Law 17-1992. The OCA is empowered to receive and investigate complaints of unfair or deceptive trade practices against consumers. In performing its functions, OCA administers the provisions of the Suffolk County Consumer Protection Law (Section 249 of the Suffolk County Code).

FN2. The vast majority of the claims range in amount between $1,000 and $2,500.

The Taibbis' counsel appeared at the OCA hearing and demanded that the proceeding be halted, failing which all participants would risk an order of contempt, as he contended the proceeding was stayed by 11 U.S.C. § 362. See Exh. E (Determination and Decision of Hearing Officer Drew, dated May 25, 1995, hereafter referred to as the "Decision") to Declaration of Janice A. Whelan, Esq., dated Oct. 6,1995 ("Whelan Decl.").

The hearing officer, after consultation with the county attorney, concluded that the proceeding was "a duly called regulatory proceeding of a governmental unit designed to enforce the Suffolk County Consumer Protection Code" and as such was excepted from the stay pursuant to 11 U.S.C. § 362(b)(4). See Exh. E to Whelan Decl. Accordingly, the hearing officer advised Debtors' counsel that the hearing would proceed in absentia, if necessary. [FN3] Debtors' counsel left, and the ***264** hearing officer thereafter took sworn testimony from witnesses. Ten days later, the hearing officer issued her Decision, which concluded as follows:

FN3. The letter sent to the Debtors by the Director of the Enforcement and Finance Division of OCA, dated April 25, 1995, to advise them of the hearing stated that "failure to appear as scheduled may occasion the Hearing to be held 'in absentia' or a default decision rendered if you fail to appear, with the assessment of such penalties as may therein be determined." See Whelan Decl., Exh. D.

"Based upon a comprehensive study and review of the information and documentatiuon [sic] contained in the record, along with the sworn testimony of the parties, it is determined that there is substantial evidence that Respondents did in fact, knowingly and deliberately mislead consumers in each instance, by engaging in deceptive and unconscionable trade practices which are prohibited by Suffolk County's Consumer Protection Law, without any mitigating factors to his behaviour. The violations are deemed founded and the maximum penalty is assessed. The maximum penalty for each violation count is $500.00. 21 COUNTS = $10,500.00 due and payable to the Suffolk County Office of Citizen Affairs by June 30, 1995. In addition, it is recommended that the Director of the Bureau of Enforcement and Finance of the Suffolk County

Office of Citizen Affairs, review the circumstances of the subject cases with the District Attorney's office for possible criminal sanctions, and with both the County Attorney and the State Attorney General for possible action vis a vis the Bankruptcy Court." [FN4]

FN4. The Debtors filed a motion on June 25, 1995, seeking to permanently enjoin the County, OCA, and the hearing officer from continuing with their investigations, hearings and other actions on the basis that the such activity was in violation of the automatic stay. The Debtors further sought an order declaring that the hearing officer's determination to be void because it was allegedly entered in violation of the stay. That motion was denied by Order of this Court, dated August 24, 1995. The Debtors did not appeal. In addition, OCA has filed a proof of claim asserting an unsecured, priority claim in the amount of $10,500, as a penalty owed to a governmental unit.

The Present Controversy

Upon the Debtors' bankruptcy filing, the time within which creditors could object to the Debtors' discharge or seek to except certain debts from discharge was fixed at August 28, 1995. All creditors were sent notice of the deadline on June 5, 1995. On August 24, 1995, OCA moved for an order granting it an extension of time to file a complaint objecting to the discharge of the Debtors or to determine the dischargeability of certain debts. That motion is the subject of the present controversy.

OCA intends to commence an adversary proceeding to except the $10,500 from discharge, and requests an extension of time to file its complaint, because it alleges that it has sixty consumer complaints against the Debtors to investigate, which will require it to interview the complainants and other witnesses. OCA wants to finish its investigation in order to determine whether it would also object to the discharge of the Debtors pursuant to 11 U.S.C. § 727 and/or object "to the discharge of the debts owed to the individual consumers pursuant to s. 523." [FN5] See Application for an Order to Extend the Time to File a Complaint, ¶ 13.

FN5. None of the creditors whose complaints were the subject of the Decision filed a timely dischargeability complaint or motion to extend time; neither did any of the other individuals listed on Schedule F.

The Debtors oppose the motion. The Court requested briefing of the issues and, following further oral argument, reserved decision. [FN6] This decision constitutes the Court's findings of fact and conclusions of law to the extent they are required.

FN6. On October 3, 1995, the Court entered an Order extending OCA's time to commence an action on behalf of itself and the individual consumers pending the submission of the additional briefs, and declaring that the individual consumers' time to commence an action under §§ 727 or 523 "has expired."

DISCUSSION

I. OCA's Standing to File a Complaint

The Debtors argue that OCA is acting beyond the scope of its authority in representing consumers individually and that its continuing efforts to seek restitution for the individuals' benefit "is outrageous conduct and should not be condoned by this Court." Affirmation of Jeffrey Heller, Esq. dated Sept. 14, 1995 ("Heller Aff."), ¶ 3. The Debtors also contend that OCA lacks standing to ***265** bring a dischargeability action on behalf of the consumers.

OCA's contentions are two-fold. First, it argues that the Suffolk County Consumer Protection Law ("CPL") and Resolution 768-1992 of the Suffolk County Legislature (by which the Legislature adopted Local Law 17-1992) provide it with statutory authority to maintain an action on behalf of the consumer creditors. Secondly, it argues that it has standing to commence an adversary proceeding under the doctrine of parens patriae.

A. Statutory Standing

Section 523(c)(1) of the Bankruptcy Code provides, in pertinent part, that

> [T]he debtor shall be discharged from a debt of a kind specified in paragraph (2), (4), (6), or (15) of subsection (a) of this section, unless, on request of the creditor to whom such debt is owed, and after notice and a hearing, the court determines such debt to be excepted from discharge ...

(emphasis added). The term "creditor" means "an entity that has a claim against the debtor that arose at the time of or before the order for relief

concerning the debtor." 11 U.S.C. § 101(10). The term "debt" is defined as "liability on a claim." 11 U.S.C. § 101(12). With respect to its desire to file a dischargeability proceeding on behalf of individual consumers, the central question is therefore whether OCA holds a "claim" sufficient to confer upon it standing to sue.

[1][2][3] The term "claim" means "right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured." 11 U.S.C. § 101(5). At this point in the development of bankruptcy jurisprudence, it is settled that when enacting these statutory provisions, Congress intended to "adopt the broadest possible definition of 'claim,' " and the meanings of the terms "debt" and "claim" are coextensive. Pennsylvania Dept. of Public Welfare v. Davenport, 495 U.S. 552, 558, 110 S.Ct. 2126, 2130-31, 109 L.Ed.2d 588 (1990) (holding that restitution obligations are claims dischargeable in chapter 13). [FN7] The phrase "right to payment" means "nothing more nor less than an enforceable obligation...." Davenport, supra, 495 U.S. at 559, 110 S.Ct. at 2131.

> FN7. Although the result in Davenport has been overruled by the 1990 amendments to chapter 13 of the Bankruptcy Code, Congress left undisturbed the Supreme Court's expansive definition of "claim." Johnson v. Home State Bank, 501 U.S. 78, 84 n. 4, 111 S.Ct. 2150, 2154 n. 4, 115 L.Ed.2d 66 (1991).

OCA contends that non-bankruptcy law, i.e., the CPL, gives it a right to seek payment on behalf of the individual consumers. The CPL provides as follows:

> § 249-1. Unfair trade practices prohibited.
>
> No person shall engage in any deceptive or unconscionable trade practices in the sale, lease, rental or loan, or in the offering for sale, lease, rental or loan, of any consumer goods or services or in the collection of debts.
>
> § 249-2. Definitions.
>
> As used in this chapter, the following terms shall have the meanings indicated:
>
> * * *
>
> COMMISSIONER--The Commissioner of Consumer Affairs. [FN8]
>
> > FN8. In 1992, the Suffolk County Department of Consumer Affairs, headed by the Commissioner, was abolished. Its "functions, duties and responsibilities" were transferred to OCA by Section 1 of Local Law No. 17- 1992. OCA was thereby established, to be headed by a Director. Accordingly, the Court interprets all references in the CPL to the Commissioner or the Department of Consumer Affairs as referring to the Director or OCA Local Law 17-1992 also sets forth a laundry list of OCA's powers and duties, including the following:
> >
> > A.) To receive and investigate complaints and initiate investigations of unfair or deceptive practices against consumers.
> >
> > B.) To hold hearings, subpoena witnesses, administer oaths, take the testimony of any person under oath and in connection therewith compel the production of any evidence relating to any matter under investigation by the Office of Citizen Affairs, provided that the Director shall obtain the written consent of the County Executive or the County Attorney before issuing a subpoena or subpoena duces tecum....
> >
> > D.) To represent the interests of consumers before federal, state and local administrative and regulatory agencies and legislative bodies....
> >
> > * * *
> >
> > I.) To report to the appropriate law enforcement agency information with respect to the violation of any federal, state, or local consumer protection law....
> >
> > K) To assist, advise, and cooperate with local, state and federal agencies to protect and promote the interests of the consumers of Suffolk County.

*266 * * *

> § 249-3. Promulgation of rules and regulations.
>
> The Commissioner may, after a public hearing, adopt such rules and regulations as may be necessary to effectuate the purposes of this chapter, including regulations defining specific deceptive or unconscionable trade practices....
>
> § 249-A. Penalty for offenses; injunctive relief.
>
> A. A violation of any provision of this chapter or of any rule or regulation promulgated hereunder shall be punishable, upon proof thereof, by the payment of a civil penalty in the sum of not more than five hundred dollars ($500.) for each such violation, to be recovered in a civil action.
>
> B. Whenever any person has engaged in any acts or practices which constitute repeated or persistent violations of any provision of this chapter or any

rule or regulation promulgated hereunder, the County Attorney, upon the request of the Commissioner, may commence an action in the name of the county for a restraining order, temporary or permanent injunction or other equitable relief. [FN9]

> FN9. OCA contends, and the Debtors do not dispute, that the Director of OCA has "directed the Suffolk County Attorney's Office to institute a non-dischargeability proceeding on behalf of the individual consumers in this matter." See Mem. of Law on Behalf of Suffolk County Executive's Office of Citizen Affairs, at 6 n. 2.

§ 249-5. Settlements.
A. In lieu of instituting or continuing action pursuant to this chapter, the Commissioner may accept written assurance of discontinuance of any act or practice in violation of this chapter. Such assurance may include a stipulation for the voluntary payment by the alleged violator of the costs of investigation for [sic] the restitution by the alleged violator to consumers of money, property or other things received from such consumers in connection with a violation of this chapter.
B. An assurance entered into pursuant to this section shall not be deemed to admit the violation unless it does so by its terms.
C. A violation of an assurance entered into pursuant to this section shall be treated as a violation of this chapter and shall be subject to all the penalties provided thereof.
(emphasis added).

[4] The CPL, together with Local Law 17-1992, therefore authorize OCA to do several things: to promulgate rules and regulations to effectuate its purposes, to hold administrative hearings, to issue subpoenas, and to take testimony under oath. Upon finding a violation, OCA is specifically empowered to seek several cumulative remedies: it may assess civil penalties for each violation and request the county attorney (upon a finding of repeated or persistent violations) to commence an action in the name of the county, seeking a restraining order, injunction or other equitable relief. In addition, in lieu of commencing or continuing such an action, OCA is specifically authorized to accept a stipulation which provides for restitution. If the stipulation is violated, OCA is authorized to treat the violation as itself a violation of the CPL. The statute does not expressly create a private right of action; all of these powers and functions are vested solely in OCA. [FN10] See In re Austin, 138 B.R. ***267** 898, 904 (Bankr.N.D.Ill.1992) (stating that "the FTC is the only party that can be considered a creditor on a claim arising from a violation of § 5(a) of the Federal Trade Commission Act. The FTC has exclusive authority to bring suit to redress violations.... There is no private right of action under the Act. Thus, the only way in which the ... Act can be enforced is for the FTC to bring actions against violators in its own name").

> FN10. To determine whether a private right of action exists where none is expressed in the statute, the courts apply a three-part test: (1) whether the plaintiff is one of the class for whose particular benefit the statute was enacted, (2) whether recognition of a private right of action would promote the legislative purpose, and (3) whether creation of such a right would be consistent with the legislative scheme. Americana Petroleum Corp. v. Northville Indus. Corp., 200 A.D.2d 646, 648, 606 N.Y.S.2d 906, 908 (2d Dep't 1994). The Court assumes, without deciding, that creation of a private right of action under the CPL would not, for the reasons stated herein, be consistent with the statutory scheme. However, several bankruptcy courts have allowed standing to various public agencies despite the fact that the statute at issue authorizes a private right of action to implement its enforcement. In re Maio, 176 B.R. 170 (Bankr.S.D.Ind.1994) (finding that the SEC had standing to maintain a dischargeability action notwithstanding the existence of a private right of action under securities law); In re Taite, 76 B.R. 764 (Bankr.C.D.Cal.1987) (State of California had standing to maintain dischargeability complaint for restitution under state law); In re Smith, 39 B.R. 690 (Bankr.N.D.Ill.1984) (attorney general had standing despite the fact that Illinois Consumer Fraud Act granted private right of action to consumers).

[5] The Court believes that the CPL provisions, together with Local Law 17- 1991, grant OCA the right to seek payment on behalf of injured consumers. First, the specific authorization to commence an action seeking "equitable relief" is broad enough to encompass an action for restitution, an equitable remedy. Mertens v. Hewitt Assoc., 508 U.S. 248, 255, 113 S.Ct. 2063, 2068, 124 L.Ed.2d 161 (1993) (interpreting phrase "other appropriate equitable relief" as allowing only actions for relief typically available in equity, such as injunction, mandamus and restitution). Secondly,

the statutory scheme as a whole implicitly recognizes OCA's ability to seek restitution, as it authorizes OCA to accept restitution as a substitute for legal action. Any other reading would render the statute unintelligible: it would mean that OCA would be permitted to discontinue an action based upon a promise of a remedy it had no right to seek in the first place. While the Court concedes that the legislature's intentions could be more clearly expressed, it is unwilling to transform inartful language into utter nonsense.

In short, OCA is authorized to enforce the CPL by assessing civil penalties and commencing an action for equitable relief and by accepting restitution. It may then sue to enforce the restitution stipulation. The Court believes that this scheme is sufficient to give OCA a right to payment-- an "enforceable obligation"--on behalf of injured consumers. [FN11] See In re Tapper, 123 B.R. 594 (Bankr.N.D.Ill.1991) (explicit statement in Illinois consumer protection statute which allowed attorney general to "bring an action in the name of The People" and to seek restitution was sufficient to confer standing to determine dischargeability). OCA's ability to enforce such claims on behalf of defrauded consumers in the state court leads this Court to conclude that it is the "creditor to whom the debt is owed" within the meaning of section 523(c)(1). In re Volpert, 175 B.R. 247 (Bankr.N.D.Ill.1994).

> FN11. As OCA has yet to file a complaint, the Court is unable to predict with certainty OCA's theory of recovery. The Court notes that the requirement that the complaint be filed by the creditor to whom the debt is owed, as set forth in § 523(c)(1), is limited to complaints filed under §§ 523(a)(2), (4), (6) or (15). Many of the cases dealing with restitution orders assert nondischargeability under § 523(a)(7). The fact that any restitution awarded may ultimately end up in consumers' hands would be immaterial under § 523(a)(7). Cisneros v. Cost Control Marketing & Sales Mgt. of Virginia, Inc., 862 F.Supp. 1531 (W.D.Va.1994), aff'd, 64 F.3d 920 (4th Cir.1995), cert. denied, --- U.S. ----, 116 S.Ct. 1673, 134 L.Ed.2d 777 (1996).

While the Court need not rely on public policy arguments to support its conclusions, strong public policy also clearly favors the instant result. The CPL codifies Suffolk County's desire to protect vulnerable consumers against unconscionable or deceptive business practices. See In re DeFelice, 77 B.R. 376 (Bankr.D.Conn.1987). DeFelice held that New York's Attorney General had standing to challenge the dischargeability of debts owed to victims of consumer fraud, notwithstanding the fact that none of the individuals had themselves filed a dischargeability complaint. The Attorney General was acting pursuant to New York Executive Law Section 63(12) (McKinney 1993), [FN12] which, he ***268** argued, empowered him to act on behalf of victims of consumer fraud and that public policy supported a grant of standing. The DeFelice Court agreed. First, the Court recited the fundamental tenet that the bankruptcy court is not to be used as a "haven for wrongdoers." Secondly, the Court distinguished In re Cannon, 31 B.R. 823 (Bankr.E.D.Mo.), aff'd, 36 B.R. 450 (E.D.Mo.1983), aff'd, 741 F.2d 1139 (8th Cir.1984), on the ground that the Missouri statute at issue there, unlike Section 63, did not authorize the Attorney General to recover restitution on behalf of individual consumers. As noted above, this Court has found that OCA is authorized to seek restitution on behalf of consumers, and thus Cannon is distinguishable here, as well.

> FN12. Executive Law Section 63(12) provides:
>
> Whenever any person shall engage in repeated fraudulent or illegal acts or otherwise demonstrate persistent fraud or illegality in the carrying on, conducting or transaction of business, the attorney general may apply, in the name of the people of the state of New York, to the supreme court of the state of New York, on notice of five days, for an order enjoining the continuance of such business activity or of any fraudulent or illegal acts, directing restitution and damages and, in an appropriate case, canceling any certificate filed under and by virtue of the provisions of section four hundred forty of the former penal law or section one hundred thirty of the general business law, and the court may award the relief applied for or so much thereof as it may deem proper.... In connection with any such application, the attorney general is authorized to take proof and make a determination of the relevant facts and to issue subpoenas in accordance with the civil practice law and rules. Such authorization shall not abate or terminate by reason of any action or proceeding brought by the attorney general under this section.
>
> ***
>
> In any case where the attorney general has authority to institute a civil action or proceeding in connection with the enforcement of a law of this

> state, in lieu thereof he may accept an assurance of discontinuance of any act or practice in violation of such law from any person engaged or who has engaged in such act or practice. Such assurance may include a stipulation for the voluntary payment by the alleged violator of the reasonable costs and disbursements incurred by the attorney general during the course of his investigation. Evidence of a violation of such assurance shall constitute prima facie proof of violation of the applicable law in any civil action or proceeding thereafter commenced by the attorney general.

The DeFelice Court further relied upon the statutory scheme and legislative history of the Bankruptcy Code itself (specifically, 11 U.S.C. §§ 362(b)(4) and (5)), which reveals a congressional intent to protect the economic welfare of consumers. "Where a governmental unit is suing a debtor to prevent or stop violation of fraud, environmental protection, consumer protection, safety, or similar police or regulatory laws, or attempting to fix damages for violation of such a law, the action or proceeding is not stayed under the automatic stay...." H.R.Rep. No. 595, 95th Cong., 1st Sess. 343, reprinted in 1978 U.S.Code Cong. & Admin. News, 5787, 5838. The DeFelice Court thus held that "it would be anomalous for a state to be permitted to institute or continue such an action but lack standing to challenge the dischargeability of the underlying debt necessary to make that action meaningful." 77 B.R. at 379. While this Court may not completely espouse the reasoning of DeFelice, which did not fully address § 523(c)(1), it finds on the facts of this case that OCA has standing.

The Debtors contend that Local Law 17-1992 and Executive Law 63 are substantially different, since section 63 explicitly authorizes the attorney general to prosecute actions in which the state is interested and allows him to ask the state court for an order enjoining the continuance of "fraudulent or illegal acts", directing restitution, and damages. The Court does not, however, find the statutes to be so substantially dissimilar as to warrant opposite results. Both statutes authorize an action in the name of the governmental entity where there are repeated consumer fraud violations. Both authorize the government to take proof and issue subpoenas, and both authorize the settlement of an action by acceptance of restitution--in fact, the CPL is more explicit in this regard.

The Debtors focus on the laundry list of OCA's powers and duties set forth in Local Law 17-1992, [FN13] and point out that critically ***269** absent is authority for OCA to represent individual consumers before the judiciary. But the Debtors' myopic vision focuses too narrowly on Local Law 17-1992 for, as the Court has found above, OCA's authority to sue on behalf of consumers springs not from the statute which merely transfers functions from the Department of Consumer Affairs to OCA, but from the CPL itself.

> FN13. The Debtors also assert that pursuant to Local Law 17-1992, OCA is organized into four divisions, none of which is a legal division. That is, Local Law 17-1992 refers to the Bureaus of Administration, Consumer Complaints, Licensing and Weights & Measures. However, the Notice of Violation sent to the Debtors was signed by the "Director, Enforcement and Finance Division." Similarly, the Decision refers to both the Enforcement and Finance Division and an "Adjudication Division." The record is devoid of any explanation, but the Court suspects that the Debtors' assertions about the organizational structure of OCA may not be quite correct.

In addition, the Debtors complain that OCA's current argument is inconsistent with the position it advocated at the hearing on the Debtors' motion to consider whether OCA's activities violated the automatic stay, and that OCA should not be permitted to change course midstream. At the prior hearing, OCA stated on the record that it was not seeking restitution on behalf of individuals, but was "performing its regulatory function, and seeking to obtain penalties per the Suffolk County Code to be paid into its general coffer." Id. at ¶ 16. While the Court acknowledges that OCA's positions may have changed since that hearing, the Court finds nothing in the CPL which makes the remedies that OCA may seek mutually exclusive. [FN14] Rather, the CPL authorizes OCA to assess penalties (in its regulatory capacity) and, upon repeated violations, to commence an action seeking restitution. That OCA had not elected to commence an action seeking restitution prior to the filing with respect to the 21 affected consumers does not extinguish its ability to commence such an action now.

> FN14. Nor does the fact that OCA may have changed its position to seek additional relief necessarily imply that the Court erred in its

> determination that the automatic stay was not violated by the continuance of the enforcement proceedings. As noted above, the CPL does not prevent the OCA from pursuing alternative or parallel courses of conduct.

The Debtors argue that OCA's enforcement of the CPL will not be hindered by denying it the ability to seek restitution on behalf of consumers, because OCA may still impose civil penalties. This argument ignores, however, the fact that the CPL authorizes OCA to undertake both pursuits, and it may well be that OCA's power to seek restitution is a more coercive, and therefore more effective, deterrent to fraudulent business practices than a $500 penalty.

Many of the cases which allow standing to public agencies have their genesis in the 1952 decision of the United States Supreme Court in Nathanson v. National Labor Relations Board, 344 U.S. 25, 73 S.Ct. 80, 97 L.Ed. 23 (1952), decided under the Bankruptcy Act. In Nathanson, the National Labor Relations Board (NLRB) obtained a pre-petition order directing the debtor to pay certain employees back pay which they had lost on account of its unfair labor practices. Thereafter, the NLRB filed a claim in the bankruptcy case, and its standing to do so became at issue. The Supreme Court held:

> We think the Board is a creditor as respects the back pay awards, within the meaning of the Bankruptcy Act. The Board is the public agent chosen by Congress to enforce the National Labor Relations Act. A back pay order is a reparation order designed to vindicate the public policy of the statute by making the employees whole for losses suffered on account of an unfair labor practice. Congress has made the Board the only party entitled to enforce the Act. A back pay order is a command to pay an amount owed the Board as agent for the injured employees. The Board is therefore a claimant in the amount of the back pay.

344 U.S. at 27, 73 S.Ct. at 82 (internal citations omitted). The rationale of Nathanson is equally applicable here.

Lastly, many of the cases which have denied standing to public agencies are distinguishable. In In re Lacy, 74 B.R. 23 (Bankr.D.Or.1987), two statutes were at issue. The first, the Oregon Racketeering Influenced and Corrupt Organizations Act, did not contain a provision authorizing the state to seek restitution. The second, the Oregon Securities Law, contained a restitution provision, but specifically granted the victims--and not the state--the right to be awarded a judgment and the right to enforce the restitution order. The case of In re Hanson, 104 B.R. 261 (Bankr.N.D.Cal.1989), concerned the certification of a class action by defrauded investors on "behalf of themselves and all others similarly situated", and not an action by a *270 governmental body pursuant to statute. In **In re Cross, 203 B.R. 456 (Bankr.C.D.Cal.**1996), the Securities and Exchange Commission had commenced an action for violations of the Securities Act and, prior to the filing, had obtained a permanent receiver for the corporate assets. The SEC also obtained a restitution order which directed the debtor to pay restitution to the receiver for distribution to defrauded investors. Upon the debtor's bankruptcy filing, both the SEC and the receiver filed dischargeability complaints. The **Cross** court held that it was the receiver, and not the SEC, which had a right to payment, and therefore held that the SEC was not the "creditor to whom the debt is owed" under section 523(c)(1).

B. Standing under the Doctrine of Parens Patriae

[6] The phrase "parens patriae," which literally means "parent of the country," refers traditionally to the role of a state as sovereign and guardian of persons under legal disability, and embodies the principle that the state must care for those who cannot take care of themselves. See Black's Law Dictionary, at 1114 (6th ed.1990). It is a doctrine of standing used to protect a government's quasi-sovereign interests such as the "health and well-being--both physical and economic--of its residents in general." [FN15] Alfred L. Snapp & Son, Inc. v. Puerto Rico ex rel. Barez, 458 U.S. 592, 607, 102 S.Ct. 3260, 3269, 73 L.Ed.2d 995 (1982).

> FN15. At least one court has held that the doctrine is available only in a common law action, and should not be used to avoid the explicit standing requirements of a statute. In re Lacy, supra, 74 B.R. 23. However, the leading case decided by the U.S. Supreme Court, Alfred L. Snapp & Son, Inc. v. Puerto Rico ex rel. Barez, 458 U.S. 592, 607, 102 S.Ct. 3260, 3268- 3269, 73 L.Ed.2d 995 (1982), applied the doctrine and granted standing to the Commonwealth of Puerto Rico under federal statutes which allowed certain labor determinations to be made "upon petition of the importing employer". The Court also stated that the

> common-law approach has "relatively little to do with the concept of parens patriae standing that has developed in American law." Id. at 600, 102 S.Ct. at 3265.

[7] To have standing under the doctrine of parens patriae, the governmental entity must establish the following elements:

(1) the state must have a quasi-sovereign interest, apart from the interests of particular private parties;

(2) there must be an injury to a substantial segment of its population; and

(3) the individuals could not obtain complete relief through a private suit.

Alfred L. Snapp, supra, at 600, 608, 102 S.Ct. at 3265, 3269; People by Abrams v. 11 Cornwell Co., 695 F.2d 34 (2d Cir.1982), modified on other grounds, 718 F.2d 22 (2d Cir.1983) (en banc).

[8] To meet the first prong of the test, OCA contends that the county has a quasi-sovereign interest in enforcing the CPL in the courts in order to protect county residents from consumer fraud. It further contends that its interest is directly linked to its attempt to block the discharge of listed debts so that a discharge does not preclude restitution to the individual consumer-creditors, and "the fact that the individual consumer-creditors would also benefit from Citizens Affairs actions does not diminish that interest." Mem. on Behalf of Suffolk County Executive's Office of Citizen Affairs, at 11. The Debtor counters that OCA is not the entity empowered or authorized to vindicate the consumer protection law in the courts. But, as set forth above, the Court disagrees and finds that OCA is charged with the enforcement of the CPL, and that it may seek such enforcement in the courts. As stated by the Supreme Court in Alfred L. Snapp:

> One helpful indicia [sic] in determining whether an alleged injury to the health and welfare of its citizens suffices to give the state standing to sue as parens patriae is whether the injury is one that the state, if it could, would likely attempt to address through its sovereign law-making powers.

Alfred L. Snapp, supra, at 607-608, 102 S.Ct. at 3269.

Here, Suffolk County has attempted to address injuries resulting from consumer fraud, by enacting the CPL and creating OCA. Accordingly, the Court finds that the County has a quasi-sovereign interest, apart from that of its residents, in ensuring the *271 consumers within its borders are protected from unfair or deceptive business practices. See In re Edmond, 934 F.2d 1304 (4th Cir.1991); In re Tapper, 123 B.R. 594 (Bankr.N.D.Ill.1991); In re Sclater, 40 B.R. 594 (Bankr.E.D.Mich.1984) (Stan Bernstein, J.) (finding that attorney general had parens patriae standing to prosecute dischargeability complaint based upon fraud under Michigan's Consumer Protection Act); In re Hemingway, 39 B.R. 619, 622 (N.D.N.Y.1983) ("[O]ne would be hard-pressed to argue that protection against consumer fraud is not a subject of vital importance to the economic well-being of the citizens of New York State").

To meet the second prong, OCA points to In re DeFelice in which the court determined that the "numerosity" element is satisfied where the state is seeking to protect the interest of 51 consumers. As OCA has received 64 complaints, it contends that it has satisfied the requirement that a substantial segment of its citizens are involved. The Court agrees. See also In re Hemingway, 39 B.R. 619 (N.D.N.Y.1983) (holding that state had parens patriae standing to prosecute dischargeability complaint on behalf of six consumers who were beneficiaries of a restitution order, and stating that "it must not be overlooked that such representation is part of a much broader scheme of consumer protection"); In re Volpert, supra, 175 B.R. at 257 ("courts must consider both the 'direct' and 'indirect' effects of an alleged injury when making this determination"; injury to 55 investors could constitute injury to "sufficiently substantial" segment of the population).

To meet the third prong, OCA points out that section 249 was enacted in recognition of the fact that victims of consumer fraud need the county's assistance to maximize their chances of recovery, and points out that a dischargeability complaint is only the first step needed to afford relief in the form of payment of their claims. It argues that it has satisfied the burden of proving that complete relief is unavailable to the individuals without the assistance of the county.

The Debtors respond that the doctrine of parens patriae does not save OCA, because individuals could have obtained relief, but chose not to do so by letting the deadline for filing complaints lapse. While this argument has certain superficial appeal,

the Court believes that it is ultimately not persuasive.

First, it is not at all clear that the consumers could have brought an action under the CPL, which does not appear to create a private right of action. See In re DeFelice, supra, 77 B.R. 376 (holding that state satisfied burden of showing that individuals could not obtain relief where statute contained no private right of action); In re Hemingway, supra, 39 B.R. 619 (same). Even if the consumers could have filed their own discharge or dischargeability complaints alleging claims under the consumer protection law, courts have granted standing to public agencies notwithstanding consumers' ability to commence their own actions. In re Edmond, supra, 934 F.2d at 1312 ("the Act's inclusion of a possible private right of action does not affect the state's ability to achieve standing under the parens patriae doctrine"); In re DeFelice, supra; In re Maio, supra, 176 B.R. 170; In re Volpert, supra, 175 B.R. 247. The reasoning supporting those decisions is even more compelling here, where the amounts awarded in any restitution order may well be too small to warrant the engagement of counsel to file an adversary proceeding. In re Volpert, supra. Lastly, it may be that some of the sixty affected consumers may have relied upon OCA to prosecute their claims by filing complaints with OCA after the bankruptcy filing instead of with the bankruptcy court. Id. (stating that injured investors had relied upon state action).

II. "Cause" for an Extension of Time

[9] The Debtors assert that after this Court ruled that OCA's continuation of the hearing after their bankruptcy filing did not violate the automatic stay, they requested OCA to re-open the case as to the 21 complaints they failed to defend, but their request was unfairly denied. They label the OCA's determination as "impermissible posturing," Heller Aff. at ¶ 16, and argue that OCA's professed need to examine individual ***272** cases is not cause to extend the time to object to discharge. The Court disagrees.

It is true that OCA could immediately file a complaint with respect to both the penalty owed to it, and with respect to any allegations arising from the 21 complaints it has already investigated. However, OCA has received 60 complaints against the Debtors--the majority of which were filed within a month or two of the bankruptcy filing--and some of which were dated after the filing. The Court sees little to be gained by requiring OCA to file an immediate complaint with respect to claims it has investigated, granting it an extension of time to investigate the others, and then requiring OCA to file a second complaint after its investigation has concluded.

In addition, the Court is unwilling to find, at this point, that the need to interview individuals is cause to grant OCA an extension of time to file a complaint under section 523, but not under section 727. The Court has no idea what facts OCA's investigation will uncover, or whether those facts would form the basis for an objection to discharge.

Accordingly, OCA has established "cause" to extend its time to file a complaint under both section 523 and section 727.

III. The Need for an Adversary Proceeding to Determine Dischargeability Pursuant to 11 U.S.C. § 523(a)(7)

Following oral argument, the Court requested supplemental submissions to address the parties' respective positions concerning the dischargeability of the civil penalty assessed pursuant to the Decision. OCA argues that the penalty constitutes a penalty payable to and for the benefit of a governmental unit and, as such, is "automatically non-dischargeable and a governmental unit is not required to institute an adversary proceeding under 11 U.S.C. § 523(c) to determine the non-dischargeability of these penalties." Letter of Janice Whelan, Esq., dated Oct. 24, 1995. The letter concludes with a request that this Court issue an Order declaring that any civil penalty which has been or will be assessed by Citizens Affairs against the debtor is automatically non-dischargeable under 11 U.S.C. §§ 523(a)(7) and 523(c).

The Debtors contend that since Fed. R. Bankr.P. 4007 [FN16] states that a complaint other than one under § 523(c)--which governs complaints under §§ 523(a)(2), (4), (6) and (15)--may be filed at any time, the inference arises that a complaint must be filed under § 523(a)(7) [FN17].

FN16. Federal Rules of Bankruptcy Procedure 4007(b) and (c) provide:

> (b) Time for Commencing Proceeding Other Than Under § 523(c) of the Code. A complaint other than under § 523(c) may be filed at any time. A case may be reopened without payment of an additional filing fee for the purpose of filing a complaint to obtain a determination under this rule. (c) Time for Filing Complaint Under § 523(c) in Chapter 7 ... Cases; Notice of Time Fixed. A complaint to determine the dischargeability of any debt pursuant to § 523(c) of the Code shall be filed not later than 60 days following the first date set for the meeting of creditors held pursuant to § 341(a). The court shall give all creditors not less than 30 days notice of the time so fixed in the manner provided in Rule 2002. On motion of any party in interest, after hearing on notice the court may for cause extend the time fixed under this subdivision. The motion shall be made before the time has expired.
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> FN17. 11 U.S.C. § 523(a)(7) provides:
> (a) A discharge under section 727 ... of this title does not discharge an individual debtor from any debt-
> ***
>
> (7) 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....

[10] The import of the Code and Rules, when read together, is that a complaint under §§ 523(a)(2), (4), (6) and (15) must be filed within 60 days following the creditors' meeting (unless a request for an extension of time was made within this period); if not, then debts of those kind are discharged. Therefore, if a creditor has any ground to except his debt from discharge under one of those subsections, he must file a timely complaint or forever lose his rights. However, § 523(c)(1) and Rule 4007(c) make clear that a creditor holding grounds to except his debt from discharge under any of the other subsections of § 523(a) need not file a complaint ***273** within 60 days, and his failure to do so will not result in the automatic discharge of the debt. Rather, the Rule provides that a complaint may be filed at any time, and the case may even be reopened for that purpose. See In re Riley, 202 B.R. 169, 177 (Bankr.M.D.Fla.1996) (holding that there is no time limit for filing complaint pursuant to Section 523(a)(7)).

[11][12] The effect is to grant the bankruptcy court exclusive jurisdiction to determine the dischargeability of debts under paragraphs (2), (4), (6) and (15) of § 523(a), but concurrent jurisdiction with respect to debts falling within the other paragraphs of § 523(a). In re Szczepanik, 146 B.R. 905 (Bankr.E.D.N.Y.1992) (Goetz, J. (ret.)). The dischargeability of debts under paragraphs other than (2), (4), (6) and (15) of § 523 may be determined at any time, in any forum. Adam Glass Service, Inc. v. Federated Department Stores, Inc., 173 B.R. 840, 843 (E.D.N.Y.1994).

[13] OCA relies upon Kelly v. Robinson, 479 U.S. 36, 107 S.Ct. 353, 93 L.Ed.2d 216 (1986), In re Taite, 76 B.R. 764 (Bankr.C.D.Cal.1987), In re Kelly, 155 B.R. 75 (Bankr.S.D.N.Y.1993), and In re Sokol, 170 B.R. 556 (Bankr.S.D.N.Y.1994), aff'd, 181 B.R. 27 (S.D.N.Y.1995), for the proposition that it need not file an adversary proceeding to determine the dischargeability of the debt owed to it under § 523(a)(7). It is true that each of those cases contains language stating that such debts are "automatically nondischargeable." However, in each case an adversary proceeding had, in fact, been filed, and each case was decided within that context. The Court therefore believes that each court used the phrase "automatically nondischargeable" somewhat loosely as dictum and, when taken out of context, the phrase implies a result which the Court believes was not intended.

The cases which have considered the issue directly have spoken virtually in unison: a creditor need not file an adversary proceeding to determine the dischargeability of debt under § 523(a)(7) within the 60 day period and, in fact, need not file one at all. Rather, the creditor is free to pursue its claim in another forum, such as a state court, which has concurrent jurisdiction. A debtor, faced with the pursuit of such a claim, may raise the discharge as an affirmative defense and the state tribunal may make its determination. Or, the debtor may return to the bankruptcy court, re-opening his case if necessary, to obtain a determination here. In re Szczepanik, supra, 146 B.R. 905.

But a creditor who fails to file an adversary proceeding, while not precluded from pursuing his debt elsewhere, is not entitled to a judicial determination by a bankruptcy court that the debt is nondischargeable. In re Ganous, 138 B.R. 110 (Bankr.S.D.Fla.1992); In re Bingham, 163 B.R.

769 (Bankr.N.D.Tex.1994). The reason for such a rule is obvious: Section 523(a)(7) only excepts from discharge debts which are payable to and for the benefit of a governmental unit, which are not compensation for actual pecuniary loss. Where the matter is disputed--regardless of whether or not a particular debt meets those two elements--it must be judicially determined, and all parties must be afforded due process before such a determination can be made. The due process required is set forth in Fed. R. Bankr P. 7001, et seq.

In short, OCA need not file an adversary proceeding to determine dischargeability under § 523(a)(7). But absent such a proceeding, this Court will not issue a judicial declaration that the debt owed to it is nondischargeable.

CONCLUSIONS

1. The Court has jurisdiction over the subject matter and the parties to this core proceeding pursuant to 28 U.S.C. § 1334 and 28 U.S.C. § 157(b)(2). Venue is proper. 28 U.S.C. § 1408.

2. OCA has standing, under 11 U.S.C. § 523(c), to commence a proceeding to determine the dischargeability of debt as set forth above.

3. OCA has standing under the doctrine of parens patriae to commence a proceeding to determine the dischargeability of debt as set forth above.

*274 4. OCA has established "cause" for an extension of time to object to discharge and/or to determine dischargeability.

5. OCA need not file an adversary proceeding in this Court to determine the dischargeability of debt pursuant to 11 U.S.C. § 523(a)(7). But absent such a proceeding, the Court declines to enter an order determining the debt to be non-dischargeable.

For all of the foregoing reasons, OCAs motion is granted. The time within which OCA may file a complaint objecting to discharge or excepting debts from discharge is fixed at November 28, 1997.

SO ORDERED.

END OF DOCUMENT