

CASE NOTES

Delaware Grants Motion for Contempt and Indicates that Incarceration Can Be Appropriate Sanction

By Marcos A. Ramos

Burtch v. Masiz et al. (In re Vaso Active Pharms., Inc.), Adv. Proc. No. 11-52005 (Bankr. D. Del. Aug. 11, 2014)

In *Burtch v. Masiz*, the United States Bankruptcy Court for the District of Delaware granted the plaintiff-trustee's motion for contempt as against a judgment-debtor who did not comply with the terms of a discovery-related order earlier entered by the court. In its opinion, the court discussed the standards for civil contempt and determined that arrest and incarceration is a permissible sanction under appropriate circumstances.

The trustee had sued the defendant to avoid and recover alleged preferential and/or fraudulent transfers and for other relief. The court entered a final judgment on the trustee's claim for constructive fraudulent transfer in the amount of \$322,927 plus prejudgment interest from and after December 29, 2009, through the date of satisfaction of the judgment. The defendant thereafter did not fully respond to the trustee's interrogatories and requests for production of documents pursuant to Fed. R. Bankr. Proc. 7069(a), and the court entered its order to compel the defendant's response to the discovery requests. The defendant did not comply with the order, and the trustee filed its motion and moved the court for the issuance of a bench warrant exercisable for the arrest and detention of the defendant to ensure the defendant's compliance with the order.

The court noted that its authority to sanction or find a party in contempt derived from three sources: (1) Bankruptcy Rule 7037; (2) the court's general equitable authority under Section 105 of the Bankruptcy Code; and (3) the court's inherent power as a federal court to sanction parties who have acted in bad faith. The court noted, however, that it must be "careful to exercise these inherent powers 'with restraint and discretion.'"

The court noted that sanctions may be used to coerce compliance or compensate for losses sustained, or for both reasons. The movant must demonstrate by clear and convincing evidence (1) that a valid court order existed, (2) about which the non-movant had knowledge and (3) the non-movant violated the terms of the order. The clear and convincing standard requires any ambiguity to be resolved in favor of the non-movant and no party should be held in contempt unless the court first gives "fair warning that certain acts are forbidden." The sanctions available to the court are "many and varied" and include fines and reimbursement in addition to "an indeterminate period of confinement." The court should "apply the least coercive sanction . . . reasonably calculated to win compliance with its orders." Typically, incarceration has been used

Bankruptcy and Insolvency Litigation Committee

as a sanction of “last resort” by bankruptcy courts within the Third Circuit while bankruptcy courts outside of the Third Circuit have imposed incarceration as a sanction for civil contempt, including when the court concludes that there is no reason to expect compliance in response to increased monetary sanction or there has been a history of noncompliance with prior orders of the court.

Here, the court found the defendant’s conduct “clearly contemptuous.” The order required the defendant to fully respond to the trustee’s discovery requests but the defendant did not comply, even though he understood that he was required to do so under the order. The court also noted that after entry of the order the defendant had failed to communicate with his attorneys in regard to the defendant’s compliance with the order and counsel thereafter had been granted leave to withdraw from representation of the defendant.

Guided by the Third Circuit’s directive to apply “the least coercive sanction reasonably calculated to win compliance,” the court determined that the defendant’s conduct had not “yet” convinced the court that the defendant would not respond to an increased monetary sanction. Accordingly, the court entered an order imposing a monetary sanction on the defendant and a requirement for the defendant to appear before the court at a specified date and time.

However, the court also included the “secondary sanction of incarceration” in its order to the extent that the defendant did not comply. As expressed by the court, “let there be no mistake. [Defendant] has exhausted the Court’s patience. Further failure to comply with this Court’s orders may result in the United States Marshal being notified to bring [Defendant] before the Court for incarceration.”

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