

1 **I. BACKGROUND**

2 The facts of this case are quite convoluted, as the parties
3 and the Bankruptcy Court have noted. (See Order at 3; Appellant's
4 Opening Brief at 4-5; Appellee's Reply Brief at 1-2.) This factual
5 complexity is, however, driven primarily by what the Bankruptcy
6 Court termed a "family fraud." (Order at 14.) That is to say, the
7 facts are only complex in so far as they tell the long and winding
8 story of the Taxe family's fraudulent lien on their own property,
9 which was meant to shield the property from creditors. (Id. at 3-
10 12; see also Appellant's Opening Brief at 4-8 (statement of facts);
11 Appellee's Reply Brief at 4-19 (same).) The Bankruptcy Court and
12 the parties have explained the story in detail after many hearings
13 and much briefing, so the Court does not labor over the details
14 here.

15 On appeal before this Court is the Bankruptcy Court's Order
16 granting the Chapter 7 Trustee's motion for \$150,000 in sanctions
17 jointly and severally against the Debtor Kathleen Kellogg-Taxe,
18 Debtor's brother-in-law Ronald Taxe, and attorneys for Kellspin,
19 Inc., Gregory Grantham and John Saba. Kellspin is a closely held
20 company of the Taxe family that was alleged to hold a senior lien
21 on real property owned by the Debtor at 10535 Vestone Way, Los
22 Angeles, California ("Vestone Property"). (Order at 2.)

23 The Trustee's sanction motion arose out of litigation in the
24 Bankruptcy Court about the Vestone Property. Debtor filed Amended
25 Schedules in her Chapter 7 bankruptcy (Debtor's fifth bankruptcy)
26 that disclosed for the first time "an undisputed secured claim of
27 \$1,465,815" for Kellspin as assignee of a judgment lien from the
28 Omni Group. (Id. at 9; Amended Schedules.) Debtor asserted in the

1 bankruptcy proceeding that the Vestone Property was subject to
2 Kellspin's lien, and that the lien was senior to the liens recorded
3 by First Federal Bank, Countrywide Financial, and Astoria Federal
4 Savings on the same property. (See Order at 9.) Debtor filed a
5 Proof of Claim for Kellspin, which Kellspin later amended when it
6 filed its own Proof of Claim. The Kellspin lien was not disclosed
7 in any prior bankruptcy or in the applications for loans from First
8 Federal Bank, Countrywide Financial, and Astoria Federal Savings.
9 (Id. at 7-9.)

10 Investigation into the alleged Kellspin lien led to the
11 Trustee filing an adversary proceeding in the Bankruptcy Court to
12 quiet title to the Vestone Property. Kellspin filed an Answer
13 claiming that Kellspin had a secured, first priority lien against
14 the Vestone Property. (Id. at 9-10.) Back in the bankruptcy
15 proceeding, Debtor fought the Trustee's motions for access to the
16 property, to employ a broker to sell the property, and to sell the
17 property free and clear of liens. Debtor alleged that these
18 actions could not be taken because of the Kellspin lien. (Id.)

19 In the end, several courts – state and federal bankruptcy
20 courts – have found the Kellspin lien to be fraudulent and that the
21 actions taken by the Kellspin attorneys and the Taxe family in
22 defense of that lien have all been in the knowing service of that
23 fraud. (Id. at 10-12, 14.) The Trustee sought sanctions against
24 Debtor, Ronald Taxe, Gregory Grantham, and John Saba for their
25 conduct in relation to the lien. (Id. at 12.) The Bankruptcy
26 Court granted the motion.

27 All the sanctioned parties appealed the Order. (Dkt. No. 2.)
28 This Order only reviews Debtor's appeal, however, because John Saba

1 and Gregory Grantham never filed an appeal brief, and Ronald Taxe's
2 late and oversized brief was struck from the docket pursuant to
3 Trustee's unopposed motion. (See Dkt. No. 45.)

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5 **II. LEGAL STANDARD**

6 The Bankruptcy Court's findings of fact are reviewed under the
7 clearly erroneous standard and conclusions of law are reviewed de
8 novo. In re Brown, 235 B.R. 644, 646 (Bankr. C.D. Cal. 1999); see
9 also In re Lazar, 83 F.3d 306, 308 (9th Cir. 1996). Awards of
10 sanctions are reviewed for an abuse of discretion. In re Lehtinen,
11 564 F.3d 1052, 1058 (9th Cir. 2009).

12 **III. DISCUSSION**

13 The sole issue on appeal is the Bankruptcy Court's imposition
14 of sanctions against Debtor. Debtor's brief states six issues on
15 appeal, but all six ask the question of whether the Bankruptcy
16 Court abused its discretion in sanctioning Debtor. (Appellant's
17 Opening Br. at 3.)

18 Debtor argues that she was not a party to the adversary
19 proceeding to quiet title to the Vestone Property and so she cannot
20 be sanctioned for actions taken in that suit. (Id. at 9-10.) She
21 also argues that the Bankruptcy Court's award of sanctions under 11
22 U.S.C. § 105 was improper and excessive, and that any sanction
23 should have been under Federal Rule of Bankruptcy Procedure 9011,
24 which is equivalent to Federal Rule of Civil Procedure 11. (Id. at
25 10-12, 22-26.) Debtor further claims that the Bankruptcy Court
26 erroneously based its ruling on a statutory section limiting a co-
27 creditor filing a proof of claim for another creditor, instead of a
28 debtor filing a proof of claim for a creditor. (Id. at 13-22.)

1 The Trustee responds that sanctions are available to the
2 Bankruptcy Court under both Rule 9011 and Section 105(a), and that
3 the use of Section 105(a) was proper here. (Appellee Reply Br. at
4 19-21.) She argues that the sanctions were meant for both the
5 Debtor's behavior in her bankruptcy proceeding as well as Ronald
6 Taxe's and the Kellspin attorneys' acts in the adversary
7 proceeding, thus it does not matter that Debtor was not a party to
8 the adversary proceeding. (Id. at 21-22.) As for the proof of
9 claim, at no point, the Trustee says, did the Bankruptcy Court
10 state that Debtor could not file a proof of claim for a creditor –
11 it simply found that Debtor's doing so was in bad faith. (Id. at
12 22-23.) Lastly, the Trustee argues that Debtor failed to show that
13 the Bankruptcy Court's finding of bad faith was clearly erroneous.
14 (Id. at 23.)

15 **A. Section 105 versus Rule 9011**

16 A bankruptcy court has sanctioning power under both Section
17 105 and Rule 9011, but the two statutes entail different standards.
18 Rule 9011 is modeled after Federal Rule of Civil Procedure 11,
19 which means it is a limited sanctioning power for attorneys or
20 unrepresented parties that make misrepresentations to the court.
21 See Fed. R. Bankr. Pro. 9011; Fed. R. Civ. P. 11. The Rule
22 requires that a party to be sanctioned receive notice and a
23 reasonable opportunity to correct the misrepresentation before
24 sanctions are granted. Fed. R. Bankr. Pro. 9011.

25 By contrast, 11 U.S.C. § 105(a) contains a broad grant of
26 inherent power:

27 The court may issue any order, process, or judgment that is
28 necessary or appropriate to carry out the provisions of
 this title. No provision of this title providing for the

1 raising of an issue by a party in interest shall be
2 construed to preclude the court from, sua sponte, taking
3 any action or making any determination necessary or
appropriate to enforce or implement court orders or rules,
or to prevent an abuse of process.

4 11 U.S.C. § 105(a). This broad grant of power includes the ability
5 to sanction bad faith conduct conducted in bankruptcy courts by a
6 party, a non-party, and attorneys. See, e.g., In re Rainbow
7 Magazine, Inc., 77 F.3d 278, 284 (9th Cir. 1996) ("There can be
8 little doubt that bankruptcy courts have the inherent power to
9 sanction vexatious conduct presented before the court." (citing 11
10 U.S.C. § 105(a))). However, in In re Dyer, 322 F.3d 1178, 1196
11 (9th Cir. 2003), the Ninth Circuit explained that there is a
12 difference between the civil contempt power of bankruptcy courts
13 under 11 U.S.C. § 105(a) and the inherent sanctioning power of
14 courts, and that earlier decisions of the Circuit had confused the
15 two. Since the issue in this case is about bad faith litigation
16 conduct, which could be upheld under either the inherent
17 sanctioning power or 11 U.S.C. § 105(a), this Court will not focus
18 on this jurisprudential point of difference.

19 Here, the Trustee alleged, and the Bankruptcy Court found, bad
20 faith conduct by Debtor, Ronald Taxe, and the Kellspin attorneys in
21 the various proceedings that involved the Vestone Property and the
22 fraudulent lien. Therefore, contrary to Debtor's assertions, the
23 use of Section 105 and/or the inherent sanctioning power instead of
24 Rule 9011 was appropriate in this case because Debtor was involved
25 in litigation concerning the fraudulent lien and took actions in
26 that litigation that the Trustee alleged were in bad faith.

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1 **B. Bad Faith**

2 Debtor argues that her conduct in asserting the existence and
3 validity of the Kellspin lien was in good faith and thus not
4 sanctionable. (Appellant's Opening Br. at 13-17, 24-25;
5 Appellant's Reply Br. at 4-5.) The Trustee argues that the
6 Bankruptcy Court considered Debtor's argument that she filed the
7 proof of claim for Kellspin in good faith based on her title report
8 investigation and the Bankruptcy Court properly found this argument
9 unpersuasive. (Appellee's Reply Br. at 21-22.) The Trustee
10 details the entire course of conduct that the Bankruptcy Court
11 found as evidence of Debtor's involvement in the fraudulent scheme
12 and of Debtor's bad faith. (Id. at 23-27.)

13 "The inherent sanction authority allows a bankruptcy court to
14 deter and provide compensation for a broad range of improper
15 litigation tactics." In re Dyer, 322 F.3d 1178, 1196 (9th Cir.
16 2003). The bankruptcy court must "make an explicit finding of bad
17 faith or willful misconduct" in order to exercise its inherent
18 sanctioning power. Id. The standard for bad faith or willful
19 misconduct is "something more egregious than mere negligence or
20 recklessness." Id. For bad faith, there must be some kind of
21 "improper purpose" or intent, and "even if the act consists of
22 making a truthful statement or a non-frivolous argument or
23 objection," there can be sanctionable conduct based on the bad
24 faith. Fink v. Gomez, 239 F.3d 989, 992 (9th Cir. 2001).

25 In this case, the Bankruptcy Court found Debtor engaged in bad
26 faith litigation conduct in her bankruptcy proceeding. The
27 Bankruptcy Court found that Debtor applied for multiple loans
28 without disclosing the alleged Kellspin lien as encumbering the

1 Vestone Property. Order at 7-8. Further, Debtor filed four prior
2 Chapter 13 bankruptcy cases, none of which disclosed the Vestone
3 Property as being encumbered by the Kellspin lien. Id. at 8-9.
4 The Kellspin lien was only disclosed in the current Chapter 7
5 bankruptcy proceeding, and only in Debtor's amended schedules. Id.
6 at 9. Debtor used this lien to object to any proposed creditor
7 settlement or action taken by the Chapter 7 Trustee that would
8 dispose of the Vestone Property because Debtor claimed this lien
9 was undisputed and senior to all the other liens on the home. Id.
10 As the Bankruptcy Court noted, Debtor filed a proof of claim for
11 Kellspin in order to thwart the Trustee's attempt to sell the
12 Vestone Property clear of any liens. Id. Even after the Trustee
13 filed a separate adversary proceeding in the Bankruptcy Court to
14 quiet title to the Vestone Property against Kellspin with evidence
15 that the lien was fraudulent, Debtor continued to use the Kellspin
16 lien to fight against any action taken by the Trustee to sell the
17 home. Id. at 10.

18 Based on these facts, and others as described in the Order,
19 the Bankruptcy Court found "that Richard Taxe, Debtor, and Ronald
20 Taxe participated in perpetuating a scheme that has been found to
21 be fraudulent by several state court rulings since 1994, when the
22 state court in the Fernandez v. Ronald Taxe, et al. case found the
23 Omni Group Judgment was part of a fraudulent scheme and therefore
24 void." Order at 14. The Bankruptcy Court found Debtor knowingly
25 engaged in bad faith by filing several documents "including at
26 least four oppositions/objections" that relied on the fraudulent
27 lien even though "a review of state court records would [have]
28 reveal[ed] that the judgment ha[d] been extinguished." Id. at 14.

1 Most revealingly, the court found that Debtor's filing of a proof
2 of claim on Kellspin's behalf asserting the lien despite Debtor
3 hiding such a lien in prior bankruptcies was in bad faith, and was
4 unnecessary as "Debtor d[id] not personally appear to be liable for
5 the underlying judgment" for the Kellspin lien. Id. at 14-15.
6 Thus, there was no benefit to the bankruptcy estate in disclosing
7 the lien or in filing a proof of claim, other than to attempt to
8 thwart the sale of the Vestone Property in settling other debts
9 that the Debtor was most certainly personally liable for. See id.
10 at 15-16.

11 The Bankruptcy Court expressly held that Debtor's conduct as
12 alleged was in bad faith:

13 Because the Debtor failed to initially disclose the
14 existence of Kellspin's lien in her schedules; because she
15 filed a very detailed but false proof of claim; and because
16 she blindly condoned and/or participated in the fraudulent
17 attempts to advance the validity of the lien during the
18 course of this case after it had been declared invalid by
19 several courts; this Court finds that the Debtor's actions
20 were done in bad faith with the intent to perpetuate a
21 fraudulent scheme to the creditors of this estate and to
22 this Court.

23 Id. at 16. Thus, based on this finding of fact and application of
24 the law to these facts, the Bankruptcy Court granted the Trustee's
25 motion for sanctions against the Debtor.

26 Debtor's argument that she was not a party to the adversary
27 proceeding where the legitimacy of the Kellspin lien was determined
28 and thus should not be sanctioned fails because as described above,
the conduct sanctioned relates to Debtor's conduct in her
bankruptcy proceeding. (See Appellant's Opening Br. at 9-10.) And
most importantly, Debtor's argument that she filed the proof of
claim for Kellspin "in good faith and after a reasonable

1 investigation and review of the title records" was properly found
2 by the Bankruptcy Court to not be true. The factual findings of
3 the Bankruptcy Court are not clearly erroneous based on the record
4 developed.

5 Debtor attempts to use Bankruptcy Code Section 501(c) to
6 demonstrate that she legally could make a proof of claim on behalf
7 of a creditor. (Appellant's Opening Br. at 17-19.) Thus, she
8 claims, the Bankruptcy Court made an error of law because it found
9 that her filing a proof of claim was part of her bad faith conduct
10 but it was expressly allowed under the Bankruptcy Code.

11 Section 501(c) does allow a debtor to file a proof of claim
12 for a creditor. 11 U.S.C. § 501(c). However, as the Bankruptcy
13 Court in this case noted, Kellspin was not a creditor of the
14 Debtor, so under Sections 501 and 502, there were no grounds for
15 the Debtor to file that proof of claim. See id. §§ 501, 502.
16 Debtor's point that the Bankruptcy Court was focused on the section
17 relating to another creditor filing a proof of claim on behalf of a
18 creditor who failed to do so is inapposite. Debtor was not in debt
19 to Kellspin, and the Kellspin lien was not a personal obligation to
20 be discharged in bankruptcy.

21 Lastly, Debtor's further arguments that she made "an
22 objectively reasonable inquiry" into the Kellspin lien fail to
23 engage with the abuse of discretion and clearly erroneous standards
24 of review that control this appellate review. (See Appellant's
25 Opening Br. at 14-15.) The Bankruptcy Court found that Debtor and
26 her family were using the Kellspin lien in furtherance of a fraud,
27 that Debtor knowingly filed a proof of claim that was false and
28 unsupported by the state court record, and that this conduct

1 amounted to bad faith. This Court can review the Bankruptcy
2 Court's findings only under the abuse of discretion and clearly
3 erroneous standards, and based on the facts found and the reasoning
4 of the Bankruptcy Court, this Court cannot find that Debtor's
5 arguments overcome this high standard.

6 **C. Amount of Damages**

7 Debtor argues that the amount of sanctions imposed are
8 disconnected from any compensatory or deterrence justification and
9 are instead motivated by an attempt to get attorneys' fees where
10 none are warranted and to coerce settlement. (Appellant's Opening
11 Br. at 22-26; Appellant's Reply Br. at 9-10.) The Trustee responds
12 that the Bankruptcy Court was presented with evidence regarding the
13 fees Trustee's attorneys incurred based on the litigation
14 surrounding the fraudulent Kellspin lien. (Appellee's Reply Br. at
15 28-29.) Thus, the Trustee argues, the amount of the sanctions was
16 based on compensatory damages as well as deterring future bad
17 conduct. (Id.)

18 The amount of damages imposed in an inherent sanction
19 authority or Section 105 case is limited to compensatory damages –
20 the Ninth Circuit has found Bankruptcy Courts and the procedures
21 they follow do not provide sufficient procedural safeguards for
22 imposing punitive damage awards. In re Dyer, 322 F.3d at 1197.

23 Here, the Bankruptcy Court awarded \$150,000 jointly and
24 severally in sanctions against Debtor, Ronald Taxe, John Saba, and
25 Gregory Gantham. John Saba, however, had the option of paying
26 \$10,000 out of his own funds to be released from the remainder of
27 the sanction award. Order at 19 n.9. This amount must be
28 justified by the purpose of compensating the Court and the Trustee

1 for the bad faith conduct of these parties. The Trustee presented
2 evidence to the Bankruptcy Court that "the fees of her attorneys in
3 the effort to combat the fraudulent Kellspin claim were in the sum
4 of \$361,595." (Appellant's Br. at 29.) These fees were not
5 limited to solely the adversary proceeding, but also included fees
6 from the bankruptcy proceeding itself. (Id.) Thus, the amount
7 awarded in sanctions is not an abuse of discretion considering the
8 amount of time and work required by the Trustee to fight the
9 fraudulent lien and the conduct committed by the parties.

10 **IV. CONCLUSION**

11 For all the reasons discussed above, this Court DENIES Debtor
12 Kathleen Kellogg-Taxe's appeal and AFFIRMS the award of sanctions.

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14 IT IS SO ORDERED.

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17 Dated: December 7, 2015


DEAN D. PREGERSON
United States District Judge

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