

JUN 26 2009

HAROLD S. MARENUS, CLERK
U.S. BKCY. APP. PANEL
OF THE NINTH CIRCUIT

NOT FOR PUBLICATION

UNITED STATES BANKRUPTCY APPELLATE PANEL
OF THE NINTH CIRCUIT

6	In re:)	BAP No.	WW-08-1299-JuHMo
)		
7	BRUCE R. YNCERA and)	Bk. No.	05-15818
	LORI J. YNCERA,)		
8)		
	Debtors.)		
9	_____)		
)		
10	JONATHAN S. SMITH,)		
)		
11	Appellant,)		
)		
12	v.)	MEMORANDUM¹	
)		
13	BRUCE R. YNCERA and)		
	LORI J. YNCERA,)		
14)		
	Appellees.)		
15	_____)		

Argued and Submitted on May 19, 2009
at Seattle, Washington

Filed - June 26, 2009

Appeal from the United States Bankruptcy Court
for the Western District of Washington

Honorable Karen A. Overstreet, Chief Bankruptcy Judge, Presiding

Before: Jury, Hollowell and Montali, Bankruptcy Judges.

¹ This disposition is not appropriate for publication. Although it may be cited for whatever persuasive value it may have (see Fed. R. App. P. 32.1), it has no precedential value. See 9th Cir. BAP Rule 8013-1.

1 Appellant Jonathan S. Smith ("Smith") appeals the
2 bankruptcy court's order that directed him to return a \$13,500
3 real estate commission to the chapter 13 trustee.² Smith's
4 primary challenge to the court's ruling is based on lack of
5 procedural due process.

6 We agree that the court's decision to impose restitution
7 did not meet minimum procedural due process standards. We
8 conclude that the bankruptcy court did not give Smith adequate
9 notice as to how and under what authority it was planning to
10 proceed nor did it give him an opportunity to address the issues
11 before entering its final order imposing restitution. These
12 deficiencies proved prejudicial.

13 Accordingly, for the reasons set forth below, we REVERSE
14 and REMAND for further proceedings consistent with this
15 decision.

16 I. FACTS

17 Bruce R. Yncera and Lori J. Yncera (collectively,
18 "Debtors") filed their chapter 13 petition on May 3, 2005 with
19 the assistance of Gregory P. Cavagnaro ("Cavagnaro").³ Debtors
20 initially tried to retain their residence as part of their

21
22 ² The three orders relevant to this appeal are dated
23 October 10, 2007, November 9, 2007 and November 7, 2008, the last
of which forms the basis of this appeal.

24 ³ Unless otherwise indicated, all chapter, section and rule
25 references are to the Bankruptcy Code, 11 U.S.C. §§ 101-1330, and
26 to the Federal Rules of Bankruptcy Procedure, Rules 1001-9037, as
27 enacted and promulgated prior to the effective date of The
28 Bankruptcy Abuse Prevention and Consumer Protection Act of 2005,
Pub. L. 109-8, 119 Stat. 23, because the case from which this
appeal arises was filed before its effective date (generally
October 17, 2005).

1 chapter 13 plan, but later decided to sell it after falling
2 behind on their post-petition mortgage payments. They entered
3 into an adequate protection order with their lender and filed an
4 amended plan providing for the sale of their residence.

5 On December 27, 2005 the bankruptcy court authorized the
6 employment of John L. Scott Real Estate as Debtors' realtor,
7 with Smith as their real estate agent and John L. Scott
8 ("Scott") as broker.

9 Debtors filed their motion to sell their residence and
10 noticed the hearing for August 2, 2006. Cavagnaro knew he was
11 going to be away on vacation on that date, but he set the
12 hearing anyway because it was the only date available which
13 allowed for a timely closing of the sale. Cavagnaro arranged to
14 have another attorney appear on Debtors' behalf, but his office
15 was notified on the eve of the sale hearing that this attorney
16 could not appear due to an illness.

17 Following this last minute cancellation, Cavagnaro's office
18 contacted Smith and asked if he could appear as Debtors'
19 attorney at the sale hearing. Smith already intended to appear
20 at the hearing to answer any questions about the sale in his
21 capacity as Debtors' real estate agent. He agreed to appear for
22 Debtors as their attorney.

23 The bankruptcy court authorized the sale of Debtors'
24 residence by order entered on August 2, 2006. The order
25 approving the sale directed, among other things, that the real
26 estate broker's commission was to be paid in full from escrow as
27 a condition of closing. The HUD-1 Settlement Statement
28 referenced in the order indicates that a \$13,500 commission was

1 payable to Scott.⁴

2 Displeased with the sale, Debtors sent a letter to the
3 bankruptcy judge, claiming that they never wanted to sell their
4 residence. They also alleged misconduct and conflicts of
5 interest on the part of Smith and Cavagnaro, argued that they
6 had improper representation at the sale hearing which caused
7 them to involuntarily give up their homestead exemption and
8 ultimately asked the court to reconsider the sale order.

9 Debtors' letter raised serious concerns regarding the
10 adequacy of their representation and the conduct of their
11 professionals. The letter alleged, among other things, that
12 Smith and Cavagnaro worked in the same office and shared an
13 improper client referral relationship. Debtors also alleged
14 that they were never comfortable with having Smith appear on
15 their behalf at the sale hearing, and that he failed to
16 represent their best interests. Debtors further claimed that
17 Smith actually did what was best for himself because, as their
18 agent, he had a pecuniary interest in real estate commissions he
19 would receive if the court approved the sale of their residence.

20 **A. The September 1, 2006 Order to Show Cause**

21 As a result of Debtors' letter, the bankruptcy court sua
22 sponte issued an Order to Show Cause ("OSC") on September 1,
23 2006. The OSC stated that the court treated Debtors' letter as
24 a motion for reconsideration of the sale order ("Debtors' Motion

25
26 ⁴ The record is ambiguous as to how and when Smith's
27 portion of the commission was paid from Scott and how much Smith
28 actually received out of this \$13,500 award. Smith states in his
declaration that after a sale closes, "my commissions are
automatically deposited into the general account of my sole
proprietorship."

1 for Reconsideration") under Fed. R. Civ. P. 60(b), incorporated
2 by Rule 9024. It further ordered Cavagnaro and Smith to appear
3 before the court on September 20, 2006 and show cause why the
4 sale of the residence was in Debtors' best interest. The court
5 required Smith to file a declaration itemizing all services he
6 performed in his capacity as Debtors' real estate agent.

7 Both Cavagnaro and Smith submitted responsive documents in
8 compliance with the OSC.⁵ After reviewing the documents filed
9 by the parties, the court determined that the issues presented
10 were far more complex than originally set forth, raising
11 concerns regarding its ability to act as a fact finder in the
12 matter.

13 **B. The September 19, 2006 Order Referring the Disciplinary**
14 **Matter to the District Court**

15 On September 19, 2006 the bankruptcy court referred the
16 matter to the Committee on Discipline ("Committee") at the
17 district court by order (the "Referral Order") pursuant to the
18 Local Rules of the United States District Court, Western
19 District of Washington, General Rule (W.D. Wash. Rule
20 GR)2(f)(5)(C).⁶ The Referral Order stated that any decisions
21

22 ⁵ Debtors never sent the chapter 13 trustee, Smith or
23 Cavagnaro a copy of their August 14, 2006 letter to the
24 bankruptcy judge. The record shows, however, that the parties
25 were aware of the letter because it was entered on the docket on
August 18, 2006 and electronic notice was sent to them. It was
also referred to in the court's OSC.

26 ⁶ W.D. Wash. Rule GR2 titled "Attorneys" is incorporated by
27 W.D. Wash. Local Bankr. Rule 9029-2. W.D. Wash. Rule
28 GR2(f)(5)(C) provides that "A grievance alleging that an attorney
has violated any of the standards of conduct specified in this

(continued...)

1 regarding an award of real estate commissions or the
2 disgorgement of any award already made were held in abeyance
3 pending the Committee's investigation and report. The court
4 struck the hearing on the OSC.⁷

5 Following the referral, the Committee conducted an
6 investigation and determined that further disciplinary action
7 against Smith should be pursued. Special disciplinary counsel
8 filed a complaint against Smith.

9 Thereafter, the record is silent for over a year as to
10 Debtors' Motion for Reconsideration or any issues concerning
11 Smith's commission.

12 **C. The October 10, 2007 Order⁸**

13 On July 16, 2007 Debtors filed a "Motion For Order
14 Directing Disbursal To Secured Creditor, Approving Fees And
15 Authorizing Hardship Discharge" ("Motion for Hardship
16 Discharge"). The Motion for Hardship Discharge did not mention
17 or raise any issues regarding Debtors' Motion for
18 Reconsideration or Smith's commission. The proof of service for
19 the motion indicated that the parties on the clerk's mailing
20 matrix were served with notice of the September 5, 2007 hearing.

21 ⁶(...continued)
22 Rule may be referred to the Committee from any ... Bankruptcy
23 Judge."

24 ⁷ On September 7, 2006 Debtors wrote a letter to Cavagnaro
25 asking him to withdraw as their attorney of record. The
26 bankruptcy court granted Cavagnaro's motion to withdraw as
27 Debtors' attorney of record as part of the Referral Order.
28 After Cavagnaro's withdrawal as of September 19, 2006, Debtors
retained Marc S. Stern ("Stern") as their new attorney of record.

⁸ Smith uses the date of October 9, 2007 for this order
which is the date it was signed rather than when it was entered.

1 Smith was not a party listed on this mailing matrix, and he was
2 not present at the hearing.

3 At the hearing, Stern reminded the bankruptcy court that it
4 had not yet ruled on Debtors' Motion for Reconsideration. The
5 court noted that this motion had not been addressed due to focus
6 on Smith's disciplinary action which, at the time, was still in
7 progress. Nonetheless, the court ruled sua sponte on Debtors'
8 motion.

9 The court ruled that it would not set aside the sale of
10 Debtors' residence to a good faith purchaser, but that it would
11 reconsider its award of Smith's commission. In that regard, the
12 court directed Smith to pay the full \$13,500 commission into the
13 court registry by order entered on October 10, 2007 (the
14 "October 10, 2007 Order").⁹ On the same date the court entered
15 a separate order granting Debtors their hardship discharge (the
16 "Hardship Discharge Order").¹⁰

17 **D. Smith's Motion for Reconsideration**

18 On November 9, 2007 Smith filed his motion for
19 reconsideration of the October 10, 2007 Order. The bankruptcy

20
21 ⁹ At the time the court issued the October 10, 2007 Order,
22 the Committee's investigation regarding Smith was ongoing. In a
23 letter to the bankruptcy judge dated September 14, 2007 (after
24 the hardship discharge hearing but before the court issued its
25 orders) special counsel James Smith expressed concerns regarding
26 the court's inclination to rule in Debtors' favor regarding their
27 hardship discharge. Special counsel explained that discovery had
28 only just begun in Smith's disciplinary action and suggested that
it might be premature to order Smith to return the commission at
that juncture.

¹⁰ Since this time, the bankruptcy court has reopened
Debtors' case and the U.S. Trustee has filed an adversary
complaint against them to revoke their hardship discharge.

1 court denied Smith's motion due to the filing of a creditor's
2 appeal of a different provision of the October 10, 2007 Order
3 and the Hardship Discharge Order, which deprived the court of
4 jurisdiction.

5 **E. The May 7, 2008 Stipulation**

6 The district court entered a stipulation on May 7, 2008
7 (the "Stipulation"), which concluded the disciplinary action in
8 that court. The Stipulation was entered under seal on the
9 bankruptcy court's docket on October 20, 2008.

10 According to the Stipulation, Smith did not obtain Debtors'
11 written consent prior to the hearing regarding the potential
12 conflict of interest created by his concurrent representation of
13 Debtors as both their attorney and real estate agent. Smith
14 also did not identify himself as the attorney for the Debtors at
15 the sale hearing.

16 Compounding these serious violations of professional
17 conduct, Smith neglected to carefully review revised schedules
18 and other documents provided to him prior to the sale hearing.
19 Had he done so, Smith would have learned that Debtors had
20 received substantial settlement proceeds arising out of an
21 adverse possession action relating to their residence, which had
22 not previously been disclosed to the court or Debtors'
23 creditors.¹¹ As a result, Smith did not disclose material facts
24 to the court. The Stipulation confirmed that Smith's

25
26 ¹¹ The record indicates that Debtors received a substantial
27 amount of funds (\$168,913.84) arising out of an action filed by
28 Lori Ycnera's mother, Virginia Duttenhefner, against Chicago
Title Insurance Company. The receipt of these funds was never
orally disclosed to the court or Debtors' creditors.

1 representation of Debtors at the sale hearing violated Rules of
2 Professional Conduct ("RPC") § 1.7(b) governing conflicts of
3 interest and RPC § 3.3 governing duty of candor toward the
4 tribunal for his failure to disclose material facts to the
5 court.

6 The Stipulation stated that Smith's conduct caused "little
7 or no actual or potential injury" and that he acted
8 "negligently". It also required Smith to pay \$12,500 in
9 attorney fees and provided that restitution, if any, may be
10 determined by the bankruptcy court.

11 **F. The November 7, 2008 Order**

12 After the district court dismissed the creditor's appeal of
13 the October 10, 2007 Order and the Hardship Discharge Order for
14 want of prosecution, the bankruptcy court was reconstituted with
15 jurisdiction to address Smith's motion for reconsideration.
16 However, the filed motion had been denied by court order and no
17 motion was pending. By this time, Smith's disciplinary
18 proceeding had concluded in the district court.

19 Notwithstanding the fact that no motion was pending, the
20 bankruptcy court sua sponte entered a final order denying
21 Smith's motion for reconsideration on November 7, 2008 (the
22 "November 7, 2008 Order") without a hearing.¹² The court ruled
23 that Smith's misconduct, as confirmed in the Stipulation, caused
24 harm to the estate and Debtors' creditors. As a result of its

25
26 ¹² The docket reflects a September 2008 motion by Stern to
27 give him access to the sealed disciplinary Stipulation so that he
28 could use it to defend Debtors in the revocation adversary
proceeding. Apparently the proceedings on this motion led the
court to rule further on Smith's motion for reconsideration even
though special counsel, not Smith, responded to Stern's motion.

1 finding of harm, the court directed Smith to make restitution by
2 returning the \$13,500 commission to the chapter 13 trustee for
3 distribution to creditors. The court concluded that Smith was
4 not prejudiced by the lack of notice of its October 10, 2007
5 Order since he never paid the funds into the registry as
6 ordered.

7 Smith timely filed this appeal. He argues that the court
8 erred in its rulings for numerous reasons. First, Smith
9 contends that the bankruptcy court did not have jurisdiction to
10 impose restitution after it referred the disciplinary action to
11 the district court. Next, he argues that he was not afforded
12 due process. Lastly, Smith maintains that the bankruptcy court
13 abused its discretion in imposing restitution.

14 **II. JURISDICTION**

15 The bankruptcy court had jurisdiction pursuant to 28 U.S.C.
16 § 1334 over this core proceeding under § 157(b)(2)(A). We have
17 jurisdiction under 28 U.S.C. § 158.

18 **III. ISSUES**

19 A. Whether the bankruptcy court had jurisdiction to
20 impose restitution on Smith after it referred his disciplinary
21 matter to the district court.

22 B. Whether the bankruptcy court afforded Smith due
23 process before issuing its order imposing restitution.

24 C. Whether the bankruptcy court abused its discretion in
25 imposing restitution on Smith.

26 **IV. STANDARDS OF REVIEW**

27 We review questions of subject-matter jurisdiction de novo.
28 Atty. Gen. of the State of Mont. v. Goldin (In re Pegasus Gold

1 Corp.), 394 F.3d 1189, 1193 (9th Cir. 2005).

2 When the procedure the bankruptcy court uses in imposing
3 restitution raises due process issues of fair notice and the
4 right to be heard, our review is de novo. See In re Brooks-
5 Hamilton, 400 B.R. 238, 245 (9th Cir. BAP 2009).

6 We review orders imposing restitution in an attorney
7 disciplinary matter for an abuse of discretion. See Peuqot v.
8 United States Trustee (In re Crayton), 192 B.R. 970, 976 (9th
9 Cir. BAP 1996). "A court abuses its discretion when it bases
10 its decision on an erroneous conclusion of law or when the
11 record contains no evidence on which it could rationally base
12 its decision." United States v. Prairie Pharmacy, Inc., 921
13 F.2d 211, 212 (9th Cir. 1990).

14 V. DISCUSSION

15 We address first Smith's challenge to the bankruptcy
16 court's jurisdiction to impose a restitution award after
17 referral of his disciplinary matter to the district court.¹³

18 Smith argues that once the bankruptcy court referred his
19 disciplinary matter to the district court, it relinquished its

20
21 ¹³ Smith refers to the restitution imposed as both
22 "sanctions" and "restitution". "Sanctions" are defined as a
23 "penalty or coercive measure that results from failure to comply
24 with a law, rule or order", while the definition of "restitution"
25 is "compensation for injury done". Blacks' Law Dictionary 1339,
26 1368 (8th ed. 2004). Here, the court's findings state that
27 restitution was appropriate for the injuries sustained by the
28 bankruptcy estate and Debtors' creditors resulting from Smith's
violations of the RPC. As such, the November 7, 2008 Order
appears to be compensatory in nature and would therefore be
restitution. Although this distinction is irrelevant to our
ruling on the issues in this appeal, it may be relevant to the
bankruptcy court's disposition of this matter on remand.

1 jurisdiction to impose restitution to the district court and
2 the Committee. Conversely, Smith argues that the district
3 court was not authorized to delegate its jurisdiction to
4 administer discipline to the bankruptcy court. Smith cites no
5 authority in support of his argument nor have we found any.

6 The disciplinary rules and discretionary referral
7 procedures set forth in W.D. Wash. Rule GR2 are not
8 jurisdictional in nature as “[o]nly Congress may determine a
9 lower court’s subject-matter jurisdiction.” Kontrick v. Ryan,
10 540 U.S. 443, 453 (2004). The W.D. Wash. Rule GR2(f) aligns
11 with this premise. Subsection (f)(2) titled “Powers of an
12 Individual Judge to Deal with Contempt or Other Misconduct Not
13 Affected” provides:

14 Nothing contained in this Rule shall be construed to
15 limit or deny the Court the powers necessary to
16 maintain control over proceedings before it ... [or]
17 from imposing sanctions for violations of the Local
18 Rules ... or other applicable statutes or rules.
19 W.D. Wash. Rule GR2(f)(2).

20 The bankruptcy court’s power to maintain control over the
21 proceedings before it or impose sanctions comes from its
22 inherent power to discipline attorneys that appear before it.
23 Price v. Lehtinen (In re Lentinen), 332 B.R. 404 (9th Cir. BAP
24 2005), aff’d, 546 F.3d 1052 (9th Cir. 2009);¹⁴ Crayton, 192 B.R.

25 ¹⁴ In Price, the Ninth Circuit observed that the court may
26 “sanction a ‘broad range’ of conduct....” under its inherent
27 authority. 546 F.3d at 1058. However, “[b]efore imposing
28 sanctions under its inherent sanctioning authority, a court must
make an explicit finding of bad faith or willful misconduct.”
Id. “[B]ad faith or willful misconduct consists of something
more egregious than mere negligence or recklessness.” Id.

1 at 976.¹⁵ Thus, contrary to Smith's assertions, the bankruptcy
2 court had authority to impose restitution on its own in
3 addition to referring the matter to the Committee. See also
4 Price, 332 B.R. at 413 (holding that the bankruptcy court had
5 authority to impose its own sanctions in addition to referring
6 the matter to the State Bar of California).

7 Moreover, there is no authority that would prohibit the
8 district court from choosing to defer the question of
9 restitution to the bankruptcy court. At the time Smith entered
10 into the Stipulation, the bankruptcy court had already entered
11 the October 10, 2007 Order, which required Smith to disgorge
12 the commission. Furthermore, the court had denied Smith's
13 motion for reconsideration of that order due to the pending
14 appeal of another provision of the October 10, 2007 Order. In
15 short, the Stipulation, which arose out of the disciplinary
16 proceeding conducted in the district court, could not serve to

17
18 ¹⁵ Under § 328(c) a court may also deny compensation for
19 services of a professional person employed under § 327 if, at any
20 time during his employment, such professional is not a
21 disinterested person, or represents or holds an interest adverse
22 to the interest of the estate with respect to the matter on which
23 the professional person is employed. However, we note that
24 §§ 327 and 328 deal with employment and compensation of
25 professionals by a trustee, which includes debtors in possession
26 in Chapter 11 through § 1107. There is nothing in the Bankruptcy
27 Code that specifically requires real estate professionals in
28 chapter 13 cases to be employed by order of the court, nor for
the court to approve their compensation. The chapter 13 trustee
did not employ Smith or Scott. No one has raised this issue, and
we presume that Smith and Scott's employment and the court's
review of the compensation reflects the practice in the Western
District of Washington. See W.D. Bankr. Local Rule 2014-1(c).
We take no position on the propriety of th practice. Of course,
were Smith's compensation as an attorney at issue, § 330(a)(4)(B)
would apply.

1 undo those actions already taken in the bankruptcy court. Nor
2 could it bind the bankruptcy court which had independent
3 jurisdiction and authority to maintain control over the
4 proceedings before it.

5 Although the bankruptcy court had discretion to make the
6 restitution award, its award was subject to the criteria set
7 forth in Crayton, 192 B.R. at 978. We consider whether (1) the
8 disciplinary proceeding was fair; (2) the evidence supported
9 the findings below; and (3) the penalty imposed was reasonable.
10 Id.

11
12 **A. Fairness of the Proceeding and Procedural Due Process**

13 Smith contends that his due process rights were violated
14 because he was never given prior notice of his alleged
15 misconduct or the opportunity to be heard prior to the court
16 issuing its order which directed him to return the commission
17 as restitution to the estate. We agree.

18 An attorney who is subject to discipline is entitled to
19 prior notice "as to the 'reach of the grievance procedure' and
20 the precise nature of the charges leveled against him." Id.
21 In addition, "the attorney is entitled to an opportunity to be
22 heard." Id. See also Mullane v. Cent. Hanover Bank and Trust
23 Co., 339 U.S. 306, 314 (1950) ("A fundamental requisite of due
24 process of law is the opportunity to be heard.").

25 No precise, all-encompassing rule captures the
26 requirements of procedural due process, but in these
27 circumstances the Ninth Circuit has noted that "ordinarily a
28 court proposing to impose sanctions notifies the person charged

1 both of the particular alleged misconduct and the particular
2 disciplinary authority under which the court is planning to
3 proceed." Miller v. Cardinale (In re DeVille), 280 B.R. 483
4 (9th Cir. BAP 2002), aff'd, 361 F.3d 539, 548 (9th Cir. 2004).
5 Recently, the Ninth Circuit observed in Price that this rule is
6 not absolute. 564 F.3d at 1060. Rather, "due process is
7 accorded as long as the sanctionee is 'provided with
8 sufficient, advance notice of exactly which conduct was alleged
9 to be sanctionable, and [was] furthermore aware that [he] stood
10 accused of having acted in bad faith.'" Id.

11 The bankruptcy court's only notice to Smith was through
12 its OSC, which did not specifically identify any particular
13 alleged misconduct or mention any disciplinary authority under
14 which the court was planning to proceed. Rather, the OSC
15 simply mentioned Debtors' letter, which alleged Smith had a
16 conflict of interest. Moreover, the OSC does not refer to
17 sanctions, restitution or disgorgement.

18 Subsequent to the OSC, the Referral Order held in abeyance
19 any determination regarding the commission pending the
20 Committee's investigation and report.

21 Over a year later, while ruling on Debtors' Motion for
22 Hardship Discharge, the court sua sponte directed Smith to pay
23 the commission into the court registry without giving Smith
24 prior notice it was going to rule on this issue. In its
25 November 7, 2008 ruling, the court dismisses Smith's lack of
26 notice of this prior hearing by finding that no prejudice
27 occurred because Smith never complied with the order.

28

1 We disagree with the court's no-harm, no-foul approach.
2 The court's October 10, 2007 Order prejudiced Smith because he
3 reasonably relied on the Referral Order, which held all
4 decisions regarding the disgorgement of the commission in
5 abeyance. Further, without notice of the October 10, 2007
6 ruling, Smith was required to file a motion for reconsideration
7 to undo the order, which imposed a higher bar to review.

8 Over a year later the court spontaneously issued the
9 November 7, 2008 Order on Smith's motion for reconsideration
10 when the Stipulation came to its attention as a result of
11 Debtors' motion to unseal it. The court relied on the language
12 in the Stipulation that reserved the issue of restitution for
13 the bankruptcy court. However, it never gave Smith notice that
14 the restitution issue would be addressed. This oversight
15 deprived him of any opportunity to address the propriety of
16 restitution in either written argument or oral presentation.
17 Hence, the November 7, 2008 order on this issue came as a total
18 surprise. In retrospect, the totality of the court's approach
19 resulted in an unfair process.

20 In short, Smith was never given his day in the bankruptcy
21 court. Accordingly, we hold that the bankruptcy court erred as
22 a matter of law in issuing its November 7, 2008 Order without
23 affording Smith procedural due process. Thus, the threshold
24 Crayton fairness factor has not been met.

25
26 **B. Remaining Crayton Factors: Evidence to Support the
Findings and Reasonableness of the Award**

27 Because of our ruling on procedural due process, any
28 ruling by us on Smith's other contentions that restitution was

1 not warranted would be based on an inadequate record. However,
2 on remand we recommend that the bankruptcy court apply the
3 Crayton standards.

4 As the record now stands, restitution based on damage to
5 the estate is questionable. The Stipulation stated that
6 Smith's conduct caused "little or no actual or potential
7 injury". Sanctions are similarly questionable, since the
8 Stipulation says he acted "negligently" and sanctions require a
9 bad faith finding. Price, 564 F.3d at 1058.

10 Moreover, the evidence in the record is ambiguous as to
11 what amount Smith received. The HUD-1 Statement for escrow
12 clearly states that the payment was sent to Scott, who was the
13 broker for the transaction.¹⁶ While Smith later declares that
14 all his commissions were deposited directly into his account,
15 there is no detail as to how much he received from this
16 transaction. Simply put, Smith should be given an opportunity
17 to present evidence on these points.

18 In sum, on remand the court may want to consider Crayton's
19 admonition that rulings of this nature be specific, reasonable,
20 and supported by the record.

21 **C. Motion For Sanctions For Filing Frivolous Appeal**

22 Debtors filed a motion on March 3, 2009 seeking sanctions
23 under Rule 8020. Debtors contend that this appeal is based on
24 a collateral attack on the Stipulation and, therefore,
25 frivolous. Since we conclude that Smith was denied due

26
27 ¹⁶ In addition, Smith's declaration filed in response to the
28 initial OSC shows that he voluntarily gave \$1500 of his
commission to Debtors.

1 process, the appeal is not frivolous. We deny Debtors' request
2 for sanctions.

3 **VI. CONCLUSION**

4 After saying in the Referral Order that disgorgement was
5 in abeyance, then sua sponte ruling on it a year later without
6 notice, the court deprived Smith of notice. This procedural
7 unfairness was compounded when – after another year gap – the
8 court issued the November 7, 2008 Order on a reconsideration
9 motion that was not even pending. Additionally, the court
10 failed to ever identify the legal basis for the restitution
11 award other than its implicit reliance on the findings in the
12 Stipulation, findings that were not even available when
13 disgorgement was first ordered.

14 For the reasons stated above, we REVERSE and REMAND to the
15 bankruptcy court for further proceedings consistent with this
16 decision.