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BANKRUPTCY - NEW YORK

In re MA Salazar Inc.

United States Bankruptcy Court, E.D. New York - December 8, 2014 - Slip Copy - 2014 WL 6888442

MA Salazar Inc. (the “Debtor”) appealed the Bankruptcy Court’s decision denying its request to hold the Incorporated Village of Atlantic Beach (the “Village”) in contempt for violating an order of the Bankruptcy Court, and for failing to obtain an order from the Bankruptcy Court regarding the applicability of the automatic stay prior to taking action against the Debtor’s property. The order in question prohibited any party from entering the Debtor’s premises.

Prepetition, the Village after extensive litigation had been authorized to demolish the Debtor’s property, as the State Court ruled that demolition was necessary to protect the public from the unsafe structure on the Debtor’s property. After the order prohibiting any party from entering the Debtor’s premises was entered, the Bankruptcy Court found that the automatic stay did not apply to the proposed acts of the Village. The Village failed to submit an order memorializing the Court’s decision, and immediately proceeded to demolish the building. In denying the request for sanctions, the Bankruptcy Court held that the automatic stay did not apply, therefore the Village could not be sanctioned based on a violation of 11 U.S.C. § 362(a). The Bankruptcy Court further held that it did not have the authority to impose sanctions based on a prior order that did not clearly set forth that the Village could be held in contempt for its failure to abide by the prior order.

The District Court reversed in part, holding that the Bankruptcy Court had inherent authority to sanction the Village for a violation of the automatic stay, and that the Bankruptcy Court had the inherent power to impose submission to its lawful mandates. Because the prior order directing parties not to enter the Debtor’s property was specific enough to put the Village on notice, and the Village’s acts violated that order, the matter would be remanded for the Bankruptcy Court to make the following determinations: whether 1) the Court ruled that the stay did not apply to the Village pursuant to section 362(b)(4), or whether the stay applied and the Court vacated the automatic stay to permit the Village to demolish the Debtor’s building, 2) whether the Village should be sanctioned for violating the order prohibiting any party from entering the Debtor’s property, and 3) whether the Village should be sanctioned for its failure to submit an order regarding the applicability of the stay prior to demolishing the Debtor’s property.

First, the Bankruptcy Court clarified that the automatic stay did not apply to the Village as its actions were taken in the exercise of its police and regulatory powers under Bankruptcy Code § 362(b)(4). Second, the Village’s violation of the order prohibiting any party from entering the Debtor’s property was not sanctionable. The Village believed in good faith that its conduct did not run afoul of this order. Its belief stemmed from the fact that the Bankruptcy Court ruled that the stay did not apply to the Village, and parties were prohibited from entering the Debtor’s property for their own protection. If anything, the Village’s actions served to further the protection of the public. In addition, the record in the case demonstrated there was honest confusion over whether this order was meant to keep the Village from demolishing the Debtor’s property once the Court ruled that the automatic stay did not apply. Third, the Village’s failure to submit an order regarding the

applicability of the automatic stay prior to demolishing the Debtor's property did not demonstrate bad faith. Without a finding of bad faith, the Village's conduct did not warrant the imposition of sanctions.

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