

For the Benefit of the Government: Exempting Civil Restitution Penalties from Discharge Under Section 523(a)(7) of the Bankruptcy Code

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Restitution is a critical law enforcement tool. It requires defendants to repay ill-gotten gains, operates to deter future wrongdoing, and may compensate victims for the harm they sustained. For these reasons and others, the Supreme Court held in Kelly v. Robinson that criminal restitution penalties are exempt from discharge under 11 U.S.C. § 523(a)(7). The Supreme Court has not ruled, however, on the dischargeability of restitution arising from civil wrongdoing, and federal courts of appeals have split regarding whether section 523(a)(7) exempts civil restitution debts as well. This Note critiques both sides of the split and argues that the Supreme Court's reasoning in Kelly provides the best test for determining when civil restitution should and should not be discharged. Specifically, it argues that courts should exempt a civil restitution obligation from discharge if the primary purpose of that debt is to promote the government's interests in effective law enforcement, rather than to ensure the monetary compensation of private parties. From Kelly, this Note derives a two-part test for determining the primary purpose of a given restitution obligation.

I. INTRODUCTION

The State's penal purposes may best be served, in many cases, by . . . requiring monetary payments to victims. Such a penal sanction works because it is a deterrent both gen-

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eral and specific; because it has rehabilitative effects; and because it communicates both to the victim and to the society at large that justice has been done. In fact, such victim payment conditions have been supported on the precise ground that they are highly effective in forcing the offender to confront, in the most tangible and measurable way, the harmful consequences of his offense. As such, these conditions may be the best available penal sanctions in some kinds of cases.¹

Restitution is a valuable tool for meting out appropriate punishment for wrongdoing.² State attorneys general recognize that restitution provides numerous benefits to the government and society.³ Restitution serves as an effective deterrent,⁴ impresses upon the offender his responsibility to others,⁵ and reduces demands on the criminal justice system.⁶ Despite all of these benefits, the viability of restitution as an option for penalizing misconduct remains uncertain. This is true because federal courts disagree about when individuals can avoid paying restitution penalties by filing for bankruptcy.⁷

1. Brief of Amici Curiae Alabama et al. at *5, *Kelly v. Robinson*, 479 U.S. 36 (1986) (No. 85-1033) (detailing the importance of restitution on behalf of thirty-five state attorneys general and other interested parties). *Kelly* is the leading authority on the discharge of restitution debts under 11 U.S.C. § 523(a)(7), the focus of this Note. This statute reads,

(a) A discharge under section 727, 1141, 1228(a), 1228(b), or 1328(b) 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, other than a tax penalty —

(A) relating to a tax of a kind not specified in paragraph (1) of this subsection; or

(B) imposed with respect to a transaction or event that occurred before three years before the date of the filing of the petition

11 U.S.C. § 523(a)(7) (2002).

2. Brief of Amicus Curiae Connecticut et al. at *6, *Pennsylvania v. Davenport*, 495 U.S. 552 (1990) (No. 89-156).

3. *Id.*

4. *Kelly v. Robinson*, 479 U.S. 36, 49 (1986) (citing Note, *Victim Restitution in the Criminal Process: A Procedural Analysis*, 97 HARV. L. REV. 931, 937-41 (1984)).

5. *Id.*

6. See Brief of Amici Curiae Alabama et al., *supra* note 1, at *8 (citing Galaway, *Toward the Rational Development of Restitution*, in *RESTITUTION IN CRIMINAL JUSTICE*, 82, 83 (J. Hudson & B. Galaway eds., 1977)).

7. See *In re Fucilo*, No. 00-36261, 2002 WL 1008935, at *10 (Bankr. S.D.N.Y. Jan. 24, 2002) (recognizing the split of opinion between the Fourth Circuit and Seventh Circuit regarding how broadly to exempt civil restitution from discharge).

In 1986, the Supreme Court decided *Kelly v. Robinson*,⁸ and provided some protection for restitution penalties in bankruptcy. In *Kelly*, the Court held that § 523(a)(7) of the Bankruptcy Code⁹ prevents debtors from discharging *criminal* restitution penalties.¹⁰ In some respects, *Kelly* eased the concerns of law enforcement officials. Certainly, the dozens of state attorneys general who pleaded with the court to protect restitution were relieved at the outcome.¹¹ Nevertheless, the decision did not fully protect the government's use of restitution because it did not cover restitution intended to penalize civil wrongdoing. What happens, for example, when an individual takes large payments from a number of families by promising to prevent foreclosure on their homes and, instead of providing that assistance, absconds with their savings?¹² Can he avoid paying a restitution penalty resulting from that fraud simply because his punishment was non-criminal?

Without explicit guidance from the Supreme Court, federal courts have split regarding when civil restitution can be discharged in bankruptcy. Some courts broadly refuse to allow debtors to discharge civil restitution obligations that are penal in nature. To these courts, § 523(a)(7) exempts all such penalties, whether they are civil or criminal.¹³ Other courts have found many civil restitution obligations to be fully dischargeable, even those that might promote the government's interests in law enforcement. These courts construe § 523(a)(7) to protect only those civil restitution obligations that benefit the government in a very specific manner.¹⁴

This Note suggests a resolution for the split of opinion regarding how to apply § 523(a)(7) to civil restitution penalties. Specifically, it posits that determining whether or not restitution should be exempt from discharge under that provision requires a two-part test aimed at determining the restitution's purpose. It ar-

8. 479 U.S. 36 (1986).

9. The Bankruptcy Code refers to Title 11 of the United States Code.

10. *Kelly*, 479 U.S. at 52.

11. See Brief of Amici Curiae Alabama et al., *supra* note 1, at *2.

12. These are roughly the facts of *In re Towers*, 162 F.3d 952 (7th Cir. 1999), discussed *infra* Part II.C.

13. See, e.g., *U.S. HUD v. Cost Control Mktg. & Sales Mgmt. of Va., Inc.*, 64 F.3d 920, 927-928 (4th Cir. 1995).

14. See, e.g., *Towers*, 162 F.3d at 953.

gues that courts should exempt a civil restitution obligation from discharge when the purpose of that debt is to provide the same benefits to the government that criminal restitution does. Courts can determine the purpose of restitution by asking the same questions that the Supreme Court addressed in *Kelly*. First, courts should look to the statute and the court order giving rise to the restitution and ask whether the debt is based on considerations of the defendant and the government's penal interests or, instead, arises out of a desire to provide compensation to the debtor's victims. Second, courts should consider the trial resulting in the restitution and ask whether victims exercised significant control over the awarding or amount of that penalty.

This "*Kelly* test" makes sense in terms of the history and the purpose of § 523(a)(7), avoids problems associated with the alternative approaches, and yields sensible results. Part II of this Note provides some background information for analyzing discharge and exemption from discharge in bankruptcy. Part III explains the split of opinion among the Circuit Courts. Part IV presents the Note's argument.

II. DISCHARGE AND EXEMPTION

Among the foremost facets of modern bankruptcy law is the individual debtor's unwaivable right to a fresh start.¹⁵ Unlike the treatment debtors received under early bankruptcy law, those who fail to meet their financial obligations today need not fear going to prison, being executed, or having their property seized or destroyed.¹⁶ Instead, many such debtors earn a second chance at success by filing a petition under the United States Bankruptcy Code and discharging their pre-petition debts.¹⁷

Historically, the treatment of delinquent debtors was "viciously punitive."¹⁸ The word "bankruptcy," suggesting the spirit of debtor-creditor relations at the time, "derives from the medieval

15. DOUGLAS G. BAIRD, *ELEMENTS OF BANKRUPTCY* 33 (3d ed. 2001).

16. *Id.* at 30–32.

17. Section 727 of the Code allows a debtor to discharge most or all of his debts and § 524 prevents creditors from trying to collect claims against the debtor following his or her discharge. 11 U.S.C. § 727 (2000); see BAIRD, *supra* note 15, at 37–40 (explaining the process and effects of the "fresh start").

18. BAIRD, *supra* note 15, at 4.

Italian custom of breaking the benches of” bankers and merchants unable to repay creditors.¹⁹ Mere property destruction, moreover, was not the worst a debtor might face. As late as the nineteenth century, debtors were commonly jailed, or worse. Under the first English bankruptcy statutes, for example, “uncooperative bankrupts were hanged.”²⁰ This harsh treatment reflects the prevailing attitude that debtors were “miscreants who deserved whatever fate befell them.”²¹

A. FRESH START

Today, debtor/creditor law is not nearly as harsh. Rather than viewing delinquent debtors as miscreants who deserve whatever harm befalls them, American bankruptcy law operates under the assumption that the average debtor is honest but unfortunate.²² In part, this notion comes from new perceptions about credit and investments. Rather than a shameful deed taken only at the height of desperation, going into debt is something Americans do every day. In large part, it is considered productive activity. Among other things, the availability of credit allows people to take calculated risks, which through entrepreneurial spirit may produce great returns for the benefit of debtors, creditors, and society alike.²³

At the same time, taking on credit entails risk, and unfortunate circumstances may thwart even the best intentions. The kitchen of a budding restaurant, for example, may be flooded in a storm, suffering damage far in excess of the owner’s insurance coverage. A small business owner’s loved one may become seriously ill, requiring medical attention beyond the scope of the family’s otherwise sufficient health plan. As a result, once optimistic entrepreneurs may become overburdened and underfunded.

19. *Id.*

20. *Id.* at 4–5. “Bankrupt” is an outmoded term referring to a debtor who is unable to repay his creditors. The term is now considered unfairly pejorative and is replaced entirely by “debtor” in legal parlance.

21. *Id.* at 30.

22. *Id.* at 4, 33.

23. See Charles G. Hallinan, *The “Fresh Start” Policy in Consumer Bankruptcy: A Historical Inventory and an Interpretative Theory*, 21 U. RICH. L. REV. 49, 64 (1986) (“[T]he encouragement of commercial risk taking was thus established as the chief organizing principle of the bankruptcy ‘fresh start’ policy.”).

Rather than punish debtors like these, or leave them to languish in their misfortune, bankruptcy law provides those who take on credit a kind of insurance policy: the opportunity for a fresh start. By filing for bankruptcy, an unfortunate debtor can discharge many or all of his debts in exchange for the property he owns.²⁴ Although such debt forgiveness may seem unfair to creditors, the fresh start serves a number of valid purposes. Among other things, it provides the debtor with a second chance to contribute to society and deters him from taking the kinds of desperate measures — such as hiding property or trying to defraud creditors — that might tempt a person with no alternative.²⁵

B. EXCEPTIONS AND EXEMPTIONS

Of course, bankruptcy law is not so naïve as to assume that *all* debtors are honest but unfortunate. On the contrary, the policy that debtors should have an opportunity for a fresh start is balanced by the old and important principle that bankruptcy should not provide a haven for wrongdoers.²⁶ While the flooded restaurant owner might garner our sympathy, the debtor who goes bankrupt through his misdeeds or handles his bankruptcy inappropriately may not. Section 727 of the Bankruptcy Code is one provision that recognizes this concern, providing a number of *exceptions* to discharge. A debtor who destroys his company's record books,²⁷ or who lies about his assets,²⁸ likely will not receive a fresh start.²⁹ In part, this is because such a debtor does not seem to deserve a clean slate. More specifically, these subsections protect the ability of bankruptcy courts to effectively administer their cases and to discourage would-be debtors from behaving irresponsibly.³⁰

24. See 11 U.S.C. § 727 (discharging debts not excepted or exempted by another Code provision).

25. See Margaret Howard, *A Theory of Discharge in Consumer Bankruptcy*, 48 OHIO ST. L.J. 1047, 1048 (1987).

26. See, e.g., *Kelly v. Robinson*, 479 U.S. 36 (1986).

27. 11 U.S.C. § 727(a)(3).

28. 11 U.S.C. § 727(a)(4).

29. See 11 U.S.C. § 727(a) (preventing debtors who have engaged in specific prohibited activity from discharging their debts).

30. The fraud exception to discharge, for example, has three primary purposes: "(i) to punish dishonest debtors; (ii) to shift the burden of such dishonesty . . . to dishonest debtors; and (iii) to deter fraudulent conduct." Steven H. Resnicoff, *Dischargeability in Bank-*

In the spirit of preventing wrongdoers from using bankruptcy to unfair advantage, there are also a number of *exemptions* from discharge, most within § 523 of the Bankruptcy Code. These provisions prevent the discharge of specific kinds of obligations, including debts for wrongs like willful or malicious injury to another,³¹ fraud or defalcation,³² and attempts to avoid paying taxes or customs duties.³³ Like the various discharge exceptions, these provisions often have the effect of denying “wrongdoers” a fresh start. Also like the discharge exceptions, their purpose is slightly more specific.³⁴ The provisions tend to protect debts that, instead of facilitating the private compensation of one party by another, operate to promote effective administration of bankruptcy cases, efficient law enforcement, and other public interests.³⁵ Just as debtors who destroy records or lie about assets damage the courts’ ability to effectively administer bankruptcy laws,³⁶ defendants who are able to escape penalties arising from fraud or malicious injury subvert the efforts of law enforcement.

III. 11 U.S.C. § 523(A)(7)

Section 523(a)(7) is one of many exemption provisions within the Bankruptcy Code. It prevents the discharge of an obligation “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.”³⁷ Congress enacted

ruptcy of Debts Incurred by “Purported Purchasers,” 64 ST. JOHN’S L. REV. 253, 255 (1990). See also *Jennen v. Hunter*, 771 F.2d 1126, 1130 (8th Cir. 1985) (explaining that “Congress established a fraud exception to discharge ‘to discourage fraudulent conduct’”) (quoting *In re Wilson*, 12 B.R. 363, 370 (Bankr. M.D. Tenn. 1981)).

31. 11 U.S.C. § 523(a)(6).

32. 11 U.S.C. § 523(a)(4).

33. 11 U.S.C. § 523(a)(1).

34. See Lawrence Ponoroff, *Vicarious Thrills: The Case for Application of Agency Rules in Bankruptcy Dischargeability Litigation*, 70 tul. L. rev. 2515, 2560 (1996) (“The debtor’s honesty has a great deal to do with the question of discharge The exceptions in Section 523, however, are more complex than that, representing a mix of policy choices and considerations”).

35. Bankruptcy Reform Act of 1999, H.R. REP. NO. 106-123(I), at 387 (1999) (“The Bankruptcy Code does not permit the discharge of certain debts whose payments are considered to be important to society [including those] . . . incurred through a debtor’s misconduct.”).

36. See *id.*

37. 11 U.S.C. § 523(a)(7) (1990).

§ 523(a)(7) to codify a judicially created exception to discharge for criminal fines, penalties, and forfeitures.³⁸ Subsequently, the Supreme Court read it to protect criminal restitution obligations as well. The Supreme Court also implicitly deemed § 523(a)(7) to protect some *civil* restitution debts but has not yet addressed the proper treatment of those obligations.³⁹ Without express guidance from the high court, federal courts of appeals have split regarding the extent to which § 523(a)(7) exempts civil restitution from discharge.

A. CRIMINAL FINES, PENALTIES, AND FORFEITURES

Congress enacted § 523(a)(7) to prevent the discharge of certain penalties. It penned that provision “against the background of an established judicial exception to discharge for criminal sentences.”⁴⁰ Under the Bankruptcy Act of 1898, traditional criminal punishments were not expressly exempt from discharge. As the Supreme Court noted in *Kelly*, “[t]he most natural construction of the Act . . . would have allowed criminal penalties to be discharged.”⁴¹ Nevertheless, most courts refused to read the act as interfering with the government’s interest in the unfettered administration of its laws.⁴² As one judge wrote in a leading case:

It may suffice to say that nothing but a ruling from a higher court would convince me that congress, by any provision of the bankruptcy act, intended to permit the discharge under its operations of any judgment rendered by a state or federal court imposing a fine in the enforcement of its criminal laws⁴³

These courts refused to read the Bankruptcy Act to undermine penal sanctions.

38. *Kelly v. Robinson*, 479 U.S. 36, 51 (1986).

39. *See Pa. Dep’t of Pub. Welfare v. Davenport*, 495 U.S. 552, 559–62 (1990) (restitution orders are not exempt from discharge under Chapter 13), *overruled by* 11 U.S.C. § 1328(a)(3).

40. *Kelly*, 479 U.S. at 46.

41. *Id.* at 44–45.

42. *Id.* at 45.

43. *In re Moore*, 111 F. 145, 149 (W.D. Ky. 1901).

B. CRIMINAL RESTITUTION

In *Kelly v. Robinson*, the Supreme Court held that § 523(a)(7) exempts criminal *restitution* penalties from discharge in addition to traditional fines, penalties and forfeitures.⁴⁴ The Court recognized that restitution is distinct from traditional penalties but ruled that the nature of most criminal restitution brings it within the language and purpose of the statute.

In *Kelly*, Carolyn Robinson pleaded guilty to larceny after wrongfully receiving welfare benefits from Connecticut.⁴⁵ In lieu of imprisonment, the Superior Court ordered her to pay monthly restitution to the state.⁴⁶ Initially, Robinson complied with the court's order, making regular restitution payments.⁴⁷ After about one year, however, she filed for bankruptcy, seeking to discharge all of her financial obligations.⁴⁸ Although Connecticut agencies knew about Robinson's bankruptcy case and could have filed objections to prevent her from receiving a fresh start, they declined to do so.⁴⁹ The Bankruptcy Court then discharged all of Robinson's debts, including the remaining restitution owed.⁵⁰

When Robinson stopped paying restitution, the Connecticut Office of Probation informed her that it considered her debt to be non-dischargeable under the Bankruptcy Code.⁵¹ In response, Robinson filed an adversary proceeding in another bankruptcy court, seeking a declaration that she no longer owed a debt of restitution to the government.⁵² That court, however, agreed with Connecticut, finding Robinson's restitution to be exempt from discharge under § 523(a)(7).⁵³ The court determined that the debt was a non-dischargeable "penalty."⁵⁴ In a case it had decided just before *In re Robinson*, the court had "specifically rejected the argument that the restitution must be deemed compensatory be-

44. *Kelly v. Robinson*, 479 U.S. 36 (1986).

45. *Id.* at 38.

46. *Id.* at 38–39.

47. *Id.* at 39.

48. *Id.*

49. *Id.* at 42.

50. *Id.*

51. *Id.* at 39–40.

52. *Id.* at 40.

53. *Id.*

54. *In re Robinson*, 45 B.R. 423, 424–25 (Bankr. Conn. 1984) (citing *In re Pellegrino*, 42 B.R. 129, 136–137 (Bankr. Conn. 1984)).

cause . . . [i]n its view, the Connecticut statute focuses ‘upon the offender and not on the victim.’”⁵⁵

On appeal, the Second Circuit reversed the Bankruptcy Court’s decision, affirming Robinson’s discharge of the restitution.⁵⁶ The court ruled against the government for two reasons. First, it decided that Connecticut should not be able to exempt a restitution penalty after the conclusion of a bankruptcy case when it could have protected the debt by objecting *during* that case.⁵⁷ Second, it argued that the purpose of the restitution seemed to be to compensate victims for “actual pecuniary loss” and, thus, was not exempt from discharge.⁵⁸

The court emphasized that Connecticut should not have to rely on § 523(a)(7) because it could have objected during Robinson’s bankruptcy case under other exemption provisions. Section 523(a)(2), for example, exempts penalties for obtaining money under false pretenses and § 523(a)(4) exempts penalties arising from fraud or larceny. Because the government did not intercede in Robinson’s case, it lost its right to object under those subsections,⁵⁹ leaving § 523(a)(7) as its only option.⁶⁰ While § 523(a)(7) remains applicable after the close of a bankruptcy case, the court was not inclined to help the state accomplish what it neglected to do before.⁶¹

The circuit court also believed that Robinson’s restitution penalty did not fit within § 523(a)(7). The court “looked to the text of the Connecticut statute to determine whether Robinson’s probation condition was ‘compensation for actual pecuniary loss’ within the meaning of § 523(a)(7).”⁶² Because the statute allowed restitution to be assessed “for the loss or damage caused,” the court

55. Kelly v. Robinson, 479 U.S. 36, 41 (1986) (citing *Pellegrino*, 42 B.R. at 137).

56. *In re Robinson*, 776 F.2d 30 (2d Cir. 1985).

57. See Kelly v. Robinson, 479 U.S. 36, 42–43 (1986) (detailing the circuit court’s reasoning).

58. *Id.* at 43.

59. Pursuant to § 523(c), objections under §§ 523(a)(2), 523(a)(4), 523(a)(6) and 523(a)(15) are forfeited if not raised in the initial bankruptcy case.

60. Section 523(a)(7) remains an option post-bankruptcy because it is not among the provisions cut short by § 523(c). See *In re Fucillo*, No. 00-36261, 2002 WL 1008935, at *7 (Bankr. S.D.N.Y. 2002).

61. As noted in *In re Towers*, 162 F.3d 952 (7th Cir. 1998), one reason for holding the government to this standard is the policy of promoting the resolution of all relevant issues in a single proceeding. *Id.* at 956. As discussed in Part II, however, the Supreme Court found practical issues to outweigh this concern. See *Kelly*, 479 U.S. 36.

62. *Kelly*, 479 U.S. at 43.

concluded that the probation condition was “compensation for actual pecuniary loss” and, therefore, not exempt from discharge under that provision.⁶³

On the government’s appeal, the Supreme Court reversed the circuit court, rejecting both of its arguments. First, it rejected the lower court’s focus on other exemption provisions, noting practical problems with that solution. Second, it rejected the court’s conclusion that the restitution was “compensatory,” holding that § 523(a)(7) exempted that debt from discharge just as it would exempt any penalty leveled with the purpose of promoting the government’s penal interests.

The Supreme Court rejected the lower court’s focus on the availability of other exemption provisions for two reasons. First, it noted that courts should not force the government to utilize other exemptions because “reliance on a right to appear and object to discharge would create uncertainties and impose undue burdens on state officials.”⁶⁴ For example, the Court noted that “differences between the elements of crimes and the provisions of § 523 frequently might hinder the application of issue preclusion,” such as when the Bankruptcy Court required proof of common law fraud, even though the state court did not.⁶⁵ Second, the Court warned that reliance on the other exemption provisions would be inadequate. As Robinson’s attorney conceded, “some restitution orders would not be protected from discharge even if the State did appear and enter an objection.”⁶⁶ The Court explained, “[A] judge in a negligent homicide case [for example] might sentence the defendant to probation, conditioned on the defendant’s paying [restitution]. It is not clear that such a restitution order would fit the terms of any of the exceptions to discharge listed in § 523 other than § 523(a)(7).”⁶⁷

The Supreme Court rejected the court of appeals’s second argument because of the nature of the restitution in question. The Court concluded that “[b]ecause criminal proceedings focus on the State’s interests in rehabilitation and punishment, rather than the victim’s desire for compensation, . . . restitution orders im-

63. *Id.*

64. *Id.* at 48.

65. *Id.* at 48 n.8.

66. *Id.* at 48.

67. *Id.* at 48–49.

posed in such proceedings operate ‘for the benefit of the State [and] . . . are not assessed ‘for . . . compensation’ of the victim.’⁶⁸ It recognized that restitution is different from the penalties that § 523(a)(7) traditionally exempts in ways that may make it seem more likely to compensate victims than to operate for the benefit of the government. “Unlike traditional fines, restitution is forwarded to the victim, and may be calculated by reference to the amount of harm the offender has caused.”⁶⁹ The Court concluded, however, that criminal restitution obligations generally are distinguishable from compensatory debts because they primarily concern benefits to the state and the situation of the defendant rather than the interests of individual victims.⁷⁰

The Court gave three reasons for deciding the discharge issue based on whether or not the restitution in question operated primarily in furtherance of the government’s law enforcement interests. First, the history of § 523(a)(7) suggests that its purpose is to prevent bankruptcy from infringing on effective law enforcement. Congress codified that provision to recognize a judicially adopted exception to discharge concerned with keeping viable the state’s ability to “formulate and enforce penal sanctions.”⁷¹ As the Court pointed out, allowing wrongdoers to discharge restitution intended to “insure the defendant will lead a law-abiding life thereafter”⁷² would deny the government the benefit of “choosing the combination of imprisonment, fines, and restitution most likely to further the rehabilitative and deterrent goals of state criminal justice systems.”⁷³ Second, the Supreme Court noted that restitution is a critical law enforcement tool:

68. *Id.* at 53.

69. *Id.* at 51–52.

70. In *Kelly* the Court states,

The criminal justice system is not operated primarily for the benefit of victims, but for the benefit of society as a whole. Thus, it is concerned not only with punishing the defender, but also with rehabilitating him. Although restitution does resemble a judgment ‘for the benefit of the victim, the context in which it is imposed undermines that conclusion. The victim has no control over the amount of restitution awarded or over the decision to award restitution. Moreover, the decision to impose restitution generally does not turn on the victim’s injury, but on the penal goals of the State and the situation of the defendant.

Id. at 52.

71. *Id.* at 47.

72. *Id.* at 49.

73. *Id.*

Restitution is an effective rehabilitative penalty because it forces the defendant to confront, in concrete terms, the harm his actions have caused. Such a penalty will affect the defendant differently than a traditional fine, paid to the State as an abstract and impersonal entity [T]he direct relation between the harm and the punishment gives restitution a more precise deterrent effect than a traditional fine.⁷⁴

Finally, the Court noted that Congress included the “benefit of a governmental unit” language in section 523(a)(7) to allow for the discharge of merely compensatory penalties, while protecting penalties that could reap the aforementioned benefits: “It seems likely that the limitation of § 523(a)(7) to fines assessed ‘for the benefit of a governmental unit’ was intended to prevent application of that subsection to wholly private penalties”⁷⁵

In order to determine the purpose of the restitution, the Court looked to the context in which it was imposed. Specifically, the Court posed two questions: (1) Did the victim exercise control over the amount of the restitution awarded or over the decision to award restitution? (2) Did the decision to impose restitution generally turn on the victim’s injury or, instead, on the penal goals of the State and the situation of the defendant? The Court posed the first question because restitution may be more likely to serve a private, compensatory purpose if the victim has great involvement in its awarding or in determining its amount. Where a victim brings an action *qui tam*, for example, it may be reasonable to assume that any awarding of restitution does not primarily operate for the benefit of the government.

The court raised the second question because it gets to the center of why some kinds of restitution should be exempt from discharge. Whereas private debts generally should be discharged as part of a debtor’s fresh start, debts that operate to punish, rehabilitate and deter wrongdoing merit protection. Where restitution primarily considers the government’s penal goals or focuses on the defendant so as to appropriately tailor the method of punishment and rehabilitation to her situation, it seems like punitive debt. Where it turns primarily on considerations of the victim,

74. *Id.* at 49 n.10.

75. *Id.* at 51.

however, it seems more likely to serve a private, compensatory purpose.

Applying this reasoning to the facts in *Kelly*, the Court determined (1) that the victim had no control over the awarding or amount of the restitution in that case, and (2) that the restitution primarily concerned the government's penal interests and turned on the situation of the defendant. The Court gave little guidance regarding how it came to the first conclusion. Presumably, it determined that taxpayers, other potential welfare recipients, the Connecticut Department of Income Maintenance, or some combination of those parties, were the victims of Robinson's crimes. Since only the attorney general brought the criminal suit resulting in Robinson's restitution, the victims seemed powerless over its creation. To resolve the second issue, the Court looked to the statute under which the trial court created the restitution in question and to the nature of the proceedings in which it was created. First, the Court determined that Robinson's restitution likely turned primarily on the penal goals of the state and on the situation of the defendant because Connecticut General Statute § 53-30(a)(9), under which the attorney general sued Robinson, focuses specifically on those ordered to pay restitution. Rather than requiring "imposition of restitution in the amount of the harm caused,"⁷⁶ "the statute provides for a flexible remedy tailored to the defendant's situation,"⁷⁷ allowing the judge to require the defendant to pay restitution "in an amount he can afford".⁷⁸

The statute authorizes a judge to impose any of eight specified conditions of probation, as well as "any other conditions reasonably related to his rehabilitation." Clause (4) of that section authorizes a judge to require that defendant "make restitution of the fruits of his offense . . . in an amount he can afford to pay." This clause does not require imposition of restitution in the amount of harm caused. Instead it provides for a flexible remedy tailored to the defendant's situation.⁷⁹

76. *Id.* at 53.

77. *Id.*

78. *Id.* at 52.

79. *Id.* at 52-53.

Next, the Court determined that the context of the proceedings giving rise to Robinson's restitution strongly suggested that the penalty served a law enforcement purpose. "The sentence following [Robinson's] criminal conviction necessarily consider[ed] the penal and rehabilitative interest of the State. Those interests are sufficient to place restitution orders within the meaning of [that statute]."⁸⁰

C. CIVIL RESTITUTION

In *Kelly*, the Supreme Court dealt only with criminal restitution. In a subsequent case, however, it implied that § 523(a)(7) could exempt civil restitution obligations from discharge as well.⁸¹ Since then, federal courts have agreed that § 523(a)(7) applies both to criminal and civil fines, penalties and forfeitures. As one court noted, "the Supreme Court has given § 523(a)(7) a broad reading, and has held that it applies to all criminal and civil penalties."⁸² Nevertheless, courts have split regarding the extent to which § 523(a)(7) exempts civil restitution from discharge.⁸³ The circuits agree as to when civil restitution is a "penalty" payable to the government and when it is "not compensation for actual pecuniary loss," but they disagree regarding how to interpret the "for the benefit of a governmental unit" language. Some courts, led by the Seventh Circuit, read that language narrowly, demanding that the government receive a pecuniary benefit from the restitution for the debt to be exempt. Others, following the Fourth Circuit, read it broadly, demanding only that restitution be "penal in nature" to fall within § 523(a)(7).

80. *Id.* at 53.

81. See *Pennsylvania Dep't of Public Welfare v. Davenport*, 495 U.S. 552, 559–62 (1990) (holding that restitution orders are not exempt from discharge under Chapter 13), *overruled by* 11 U.S.C. § 1328(a)(3).

82. *U.S. HUD v. Cost Control Mktg. & Sales Mgmt. of Va.*, 64 F.3d 920, 927–928 (4th Cir. 1995).

83. See, e.g., *In re Fucilo*, No. 00-36261, 2002 WL 1008935, at *10 (Bankr. S.D.N.Y. 2002) ("This Court acknowledges that some courts [unlike the Fourth Circuit] have developed a restrictive view of the dischargeability of a restitution award") (citing *In re Towers*, 162 F.3d 952 (7th Cir. 1999) and *In re Rashid*, 210 F.3d 201, 208 (3d Cir. 2000)).

1. *Fine, Penalty, or Forfeiture*

Federal courts agree that restitution obligations meet the threshold requirement of § 523(a)(7). As the Supreme Court noted in *Kelly*, that provision “creates a broad exception for *all penal sanctions*, whether they be denominated fines, penalties, or forfeitures,”⁸⁴ and the forced payment of restitution is clearly a “penalty.” The federal courts of appeal have followed this reading. In *In re Towers*, for example, the Seventh Circuit noted that it is “easy enough to call restitution owed under the Illinois Consumer Fraud and Deceptive Business Practices Act ‘a fine, penalty or forfeiture’”⁸⁵ and, in *U.S. HUD v. Cost Control Marketing & Sales Management of Virginia*, the Fourth Circuit found restitution leveled under the Interstate Land Sales Full Disclosure Act to meet that requirement as well.⁸⁶

2. *Not Compensation for Actual, Pecuniary Loss*

In *Kelly*, the Supreme Court clarified that Congress added “two qualifying phrases” to the § 523(a)(7) threshold requirement: (1) “fines must be both [payable] ‘to and for the benefit of a governmental unit,’ and (2) ‘not compensation for actual pecuniary loss.’”⁸⁷ Although federal courts of appeals have split regarding when restitution operates “for the benefit of” the government, they agree on the meaning of the second qualification. Their definition of “not compensation for pecuniary loss” seems slightly different from the Supreme Court’s understanding of that element, but is applied consistently across the circuits.

Addressing Robinson’s restitution obligation in *Kelly*, the Supreme Court explained that her debt operated for the benefit of the government and, thus, was not “assessed ‘for . . . compensation’ of the victim” because “the sentence following a criminal conviction necessarily considers the penal and rehabilitative interests of the State.”⁸⁸ “Those interests,” it wrote, are “sufficient to place restitution orders within the meaning of

84. *Kelly v. Robinson*, 479 U.S. 36, 51 (1986) (emphasis added).

85. *In re Towers*, 162 F.3d 952, 954 (7th Cir. 1998).

86. *Cost Control Mktg. & Sales Mgmt. of Va.*, 64 F.3d at 928.

87. *Kelly*, 479 U.S. at 51.

88. *Id.* at 53.

§ 523(a)(7).”⁸⁹ Thus, the Court read “for the benefit” and “not compensation” to function in the alternative — either a debt serves primarily to benefit the government’s interests in rehabilitation and punishment, or it operates mainly to compensate victims for pecuniary loss.

The circuit courts have held the Supreme Court’s interpretation of “not compensation” to be slightly more specific than is apparent from the text of that opinion. Both the Seventh and Fourth Circuits, for example, deemed that language only to preclude debts serving to compensate the *government* for *its* pecuniary loss. In *Towers*, the Seventh Circuit wrote: “As [the Supreme Court] observed, restitution usually is not compensation for *the government’s* pecuniary loss. Governments seek restitution to promote law enforcement by deterrence as well as by compensation.”⁹⁰ The Fourth Circuit explained,

[T]he “not compensation for actual pecuniary loss” phrase in § 523(a)(7) refers to *the government’s* pecuniary loss. For example, a person drives recklessly and collides with a city garbage truck. A city policeman issues him a traffic ticket, and the city attorney files a negligence suit and obtains a judgment for the amount of damage to the garbage truck. The person can discharge the judgment for damaging the truck, but he cannot discharge his reckless driving fine.⁹¹

By this reasoning, payment on a debt is not exempt from discharge if it only benefits the government by providing compensation for pecuniary loss.

3. Payable for the Benefit of the Government

The source of tension among federal courts regarding the application of § 523(a)(7) to civil restitution penalties involves the first qualification to that provision’s broad protection of fines, penalties and forfeitures. Whereas courts agree about how to treat the other elements of the statute, the Fourth and Seventh Circuits differ considerably regarding when civil restitution pen-

89. *Id.*

90. *In re Towers*, 162 F.3d at 955 (1999).

91. *Cost Control Mktg. & Sales Mgmt. of Va.*, 64 F.3d at 928.

alties operate “for the benefit of” the government. In *Cost Control Marketing & Sales Management of Virginia*, the Fourth Circuit found that civil restitution provides benefits to the government for the purposes of § 523(a)(7) so long as the obligation is “penal in nature,” holding that the government *benefits* in that situation because “restitution ensures compliance with the Act and safeguards the public interest in such compliance.”⁹² In *Towers*, the Seventh Circuit relied on a very different interpretation, finding that civil restitution only meets the first qualification of the statute if it provides a pecuniary benefit to the government. The *Towers* court held that “benefits” like “deterrence” are insufficient to place restitution within § 523(a)(7) and, moreover, are costly to the government. Among other courts that have addressed the issue, most prefer a broader reading of “benefits” that recognizes deterrence, rehabilitation and other law enforcement interests. At least one court of appeals, however, suggested a preference for *Towers*.

a. Fourth Circuit

In 1989, the Department of Housing and Urban Development (“HUD”) filed suit against four officers of a real estate management company, Cost Control Marketing and Sales Management of Virginia (“CCMV”), under the antifraud provisions of the Interstate Land Sales Full Disclosure Act (the “ILSFDA”).⁹³ Over the course of three years, CCMV purchased roughly 1000 lots within a large Virginia subdivision and sold more than half of them without ever making efforts to comply with the ILSFDA.⁹⁴ On the contrary, the defendants “relied on high-pressure, misleading marketing techniques . . . to sell lots at over three times their as-

92. *Id.* at 927.

93. Initially, HUD sued CCMV in addition to suing the company’s officers. After the final order against the defendants inadvertently excluded the company, however, HUD only pursued the judgment as to the individual defendants. *Id.* at 925 n.6. Courts make no distinction between restitution created pursuant to federal law rather than state law. *In re Towers*, 217 B.R. 1008, 1012 (N.D. Ill. 1998).

94. “In particular, the defendants (1) failed to file with the plaintiff a Statement of Record in violation of 15 U.S.C. § 1703(a)(1)(A); (2) sold lots without providing purchasers with Property Reports, *id.* at § 1707; and (3) engaged in fraudulent sales practices, in violation of both the Act’s ‘anti-fraud provisions,’ *id.* § 1703(a)(2)(B), (C) and the Act’s revocation requirements, *id.* § 1703(b),(c).” *Cisneros v. Cost Control Mktg. & Sales Mgmt. of Va.*, 862 F. Supp. 1531, 1533 n.2 (W.D. Va. 1994), *aff’d*, 64 F.3d 920 (4th Cir. 1995).

essed value.”⁹⁵ In response, HUD sued the CCMV officers in the Western District of Virginia, seeking an injunction from further violations and a disgorgement of all profits gained as a result of their scheme.⁹⁶ In 1990, the district court entered a preliminary injunction against the defendants.⁹⁷ On remand, the district court entered a permanent injunction and held that restitution would be an appropriate part of their punishment, ordering the individual defendants “to make an initial payment of \$100,000, and that they be made jointly and severally liable for whatever final figure the court determined after further proceedings.”⁹⁸ Following the court’s initial order, but before final determination of the restitution amount, the CCMV officers each filed voluntary bankruptcy petitions and three of the officers received a full discharge.⁹⁹

Less than a year later, HUD filed a motion for entry of final judgment. In *Cisneros v. Cost Control Mktg. and Sales Mgmt. of Va., Inc.*,¹⁰⁰ the Western District of Virginia held that the restitution payable to HUD clearly fell within the scope of § 523(a)(7).¹⁰¹ The court ruled that, because the restitution ordered against the CCMV defendants was “penal in nature,” it fell within the statute.¹⁰² Penal restitution operates “for the benefit of the government,” it noted, “because restitution ensures compliance with the Act and safeguards the public interest in such compliance. “To permit the retention of . . . illicit profits . . . would impair the full impact of the deterrent force that is essential if adequate enforcement of [the Act] is to be achieved.”¹⁰³ The court noted that some of the restitution paid to HUD might be passed on to victims, but decided that this did not make the penalty any less payable “for the benefit of a governmental unit”:

95. *Cost Control Mktg. & Sales Mgmt. of Va.*, 64 F.3d at 923–26.

96. *Id.* at 924.

97. *Id.*

98. *Kemp v. Cost Control Mktg. & Sales Mgmt. of Va.*, 790 F. Supp. 1275, 1281 (W.D.Va. 1992).

99. *Cost Control Mktg. & Sales Mgmt. of Va.*, 64 F.3d 920 at 925.

100. 862 F. Supp. 1531 (1994).

101. *Id.* at 1534.

102. *Id.*

103. *Id.* (quoting *SEC v. Petrofunds, Inc.*, 420 F. Supp. 958, 960 (S.D.N.Y. 1976)).

The money will be paid to [HUD] rather than the injured victims, and the judgment will punish the defendants for violations of the Act and deter future violations by the defendants and others. Whether any of the money reaches the victims is immaterial to the § 523(a)(7) analysis.¹⁰⁴

On the defendants' appeal, the Fourth Circuit affirmed that § 523(a)(7) exempted the restitution in that case from discharge. In *Cost Control Mktg. and Sales Mgmt. of Va.*, the court recognized that the defendants' obligation to pay the Department of Housing might seem intended to benefit CCMV's *victims*, rather than the government: "HUD . . . often stated . . . that it intend[ed] to use some or all of its recovery to reimburse . . . purchasers."¹⁰⁵ Nevertheless, the Fourth Circuit found the restitution in that case to operate for the benefit of the government as required by the statute. In addition to "the reasons given by the district court,"¹⁰⁶ the Fourth Circuit found the restitution to be "beneficial," reading *Kelly* to hold that "it makes no difference that injured persons may . . . receive compensation" so long as the restitution in question is "penal."¹⁰⁷ The court also noted that the restitution might not be as victim-focused as initially suggested because even if HUD intended to pass restitution onto victims, "the final judgment order[ed] payment to HUD and impose[d] no obligation on HUD to disburse the money to anyone."¹⁰⁸

b. Seventh Circuit

In *Towers*, the Seventh Circuit Court of Appeals took a very different approach. Whereas the Fourth Circuit exempted the restitution in *Cost Control Mktg. and Sales Mgmt. of Va.*, because its "penal nature" would provide benefits like deterrence to the government, the Seventh Circuit refused to exempt restitution where the government would not receive a pecuniary benefit from payment on the debt.

104. *Id.*

105. *Cost Control Mktg. & Sales Mgmt. of Va.*, 64 F.3d at 927.

106. *Id.*

107. *Id.* at 928.

108. *Id.* at 927.

During the 1980s, James Towers ran a scheme to defraud homeowners in Illinois.¹⁰⁹ In return for an application fee, Towers promised that he would seek mortgage refinancing to stave off impending foreclosures.¹¹⁰ He also promised to put the fees he collected into an escrow account to be returned if refinancing attempts failed.¹¹¹ Towers, however, was not true to his word.¹¹² He bilked the homeowners of their fees without ever providing refinancing assistance or placing payments into escrow.¹¹³

In 1986, the Attorney General for the State of Illinois sued Towers under the Illinois Consumer Fraud and Deceptive Business Practices Act.¹¹⁴ The trial court found for Illinois, ordering Towers to pay restitution of about \$210,000 and to reimburse the state for \$50,000 in costs accrued while investigating his mischief.¹¹⁵ Towers later filed two separate bankruptcy cases under Chapter 7 and received a fresh start.¹¹⁶ Thereafter, the Attorney General filed a proceeding in bankruptcy court, seeking a declaration that the restitution penalties stemming from Tower's misconduct were "non-dischargeable" under § 523(a)(7).¹¹⁷ The Bankruptcy Court refused the Attorney General's request and affirmed Towers's full discharge.¹¹⁸ Although the United States District Court for the Northern District of Illinois reversed in part,¹¹⁹ the Seventh Circuit also refused to exempt the restitution from discharge.¹²⁰ The Seventh Circuit declined to exempt Towers's restitution obligation, *inter alia*, because it read the "for the benefit" language of § 523(a)(7) to require restitution to yield pecuniary gains to the government and saw no such benefits in that case.¹²¹

109. *In re Towers*, 162 F.3d 952, 953 (7th Cir. 1998).

110. *Id.*

111. *Id.*

112. *Id.*

113. *Id.*

114. *Id.*

115. *Id.*

116. *Id.*

117. *Id.*

118. *Id.* at 953–54.

119. Bankruptcy Court determinations are appealed to Bankruptcy Appellate Panels (if the jurisdiction has such a panel, which Illinois does not) or to Federal District Courts. 28 U.S.C. § 158 (1994).

120. *Towers*, 162 F.3d at 956

121. *Id.* at 955–56.

The court determined that § 523(a)(7) must require pecuniary benefits because of the statute's specific wording. "The [phrase] in which 'benefit' appears — 'payable to and for the benefit of a governmental unit' — implies that the 'benefit' in question is the benefit of the money that is 'payable to' the governmental unit."¹²² The Seventh Circuit acknowledged that some courts, including *Kelly*, recognized non-monetary benefits in the § 523(a)(7) analysis, but declined to accept those benefits for three reasons. First, the *Towers* court noted that, in *Pennsylvania Department of Public Welfare v. Davenport*,¹²³ the Supreme Court "implied in dictum that *Kelly* is applicable to civil restitution orders."¹²⁴ Nevertheless, it suggested that *Kelly's* focus on non-monetary benefits arose solely out of the criminal context and thus was inapplicable to an analysis of § 523(a)(7) regarding civil restitution debts.¹²⁵ Second, the Seventh Circuit argued that the government does not actually benefit from deterrence and other aspects of restitution penalties recognized by *Kelly* and *Cost Control Mktg. & Sales Mgmt. of Va.* because those "benefits" are costly to governmental units:

Perhaps one could reply that the state's benefit need not be pecuniary. Deterrence of fraud is a benefit to all of the state's citizens. If restitution adds to the punch of criminal law, then so much the better. Some language in *Kelly* suggests this possibility [However], the "governmental unit" does not receive any benefit from general deterrence Although potential victims gain from improved deterrence, governmental bodies experience the process as a cost — not only the outlay needed to achieve deterrence but also the possibility that, if the level of crime falls, then the budget of those governmental units devoted to crime suppression may decline.¹²⁶

122. *Id.* at 956.

123. 495 U.S. 552, 562 (1990).

124. *Towers*, 162 F.3d at 954.

125. *Id.* ("Kelly dealt with a criminal restitution order . . . its animating concern was limited to criminal cases.")

126. *Id.* at 956.

Finally, the Seventh Circuit declined to read the “for the benefit” language to include non-monetary benefits because it did not believe it needed to do so to protect the government’s ability to promote effective law enforcement:

If there were no way to protect the deterrence effects of restitution except by hammering away at “for the benefit of” until it fit the mold, then a court might be tempted. But it is not necessary. Section 523(a)(2) prevents the discharge of debts attributable to fraud (as Towers’s debts were); § 523(a)(4) exempts debts that stem from embezzlement or larceny; § 523(a)(6) exempts debts that stem from “willful and malicious injury” The only reason Illinois . . . cannot take advantage of these exclusions from discharge is that [it] snoozed through his bankruptcies.¹²⁷

After concluding that § 523(a)(7) would only exempt restitution penalties providing the government with *pecuniary* benefits, the Seventh Circuit refused to exempt Towers’s restitution from discharge. The court advanced two theories regarding why Illinois would not receive a monetary benefit from protecting Towers’s restitution. First, it argued that the Illinois Attorney General had no choice but to pass all of the restitution directly to victims.¹²⁸ It contrasted this fact with the situations in *Kelly* and *Cost Control Mktg. & Sales Mgmt. of Va.*:

In *Kelly* the governmental unit kept the restitution, for the state was itself the victim (the crime was welfare fraud). In *CCMV*, the Department of Housing and Urban Development collected the restitution and . . . was not under any legal obligation to distribute the money to persons harmed by the defendant’s acts.¹²⁹

Second, the court asserted that, irrespective of the government’s obligations, exempting Towers’s restitution from discharge would not provide a pecuniary benefit because the state would use the restitution to help Towers’s victims:

127. *Id.*

128. *Id.* at 955.

129. *Id.*

[T]he judge did not state in so many words that the Attorney General must redistribute to the victims whatever can be squeezed out of Towers. No one doubts, however, that the Attorney General *will* distribute the money to the victims; its brief informs us that “the State intends to forward restitution payments to the victims if it succeeds in collecting from Towers” and that “the State is receiving no pecuniary benefit” from this activity.¹³⁰

Either because the Attorney General was forced to pass money onto victims or because he intended to do so, the Seventh Circuit held, “Civil restitution under the Illinois Consumer Fraud and Deceptive Business Practices Act is payable to, but not for the benefit of, the Attorney General of Illinois.”¹³¹

c. Other Courts

Since the Fourth and Seventh circuits reached the decisions discussed, *supra*, few courts have addressed the proper application of § 523(a)(7) to civil restitution obligations. Among those that have, the Southern District of New York recognized the split between *Towers* and *Cost Control Mktg. & Sales Mgmt. of Va.*, citing a preference for the latter in *In re Fucilo*.¹³² In *In re Rashid*,¹³³ the Third Circuit suggested a preference for the reasoning in *Towers*.

IV. A SENSIBLE TEST FOR EXEMPTING CIVIL RESTITUTION

This Note suggests a resolution for the split of opinion among the federal circuit courts regarding when civil restitution should be exempt from discharge under § 523(a)(7) of the Bankruptcy Code. It argues that courts should follow the same approach that the Supreme Court applied to criminal restitution in *Kelly*, the “*Kelly* test.” The *Kelly* test is the logical approach given that § 523(a)(7) applies to civil restitution as well as criminal restitution. Moreover, the *Kelly* test is consistent with the purpose and legislative history of the statute, avoids significant problems as-

130. *Id.*

131. *Id.* at 956.

132. No. 00-36261, 2002 WL 1008935, at *10 (Bankr. S.D.N.Y. Jan. 24, 2002).

133. 210 F.3d 201 (3d Cir. 2000).

sociated with the approaches employed by the Fourth and Seventh Circuits, and would have provided sensible results if applied to the facts of *Towers* and *Cost Control Mktg. and Sales Mgmt. of Va.*

A. THE *KELLY* TEST APPLIES TO CIVIL RESTITUTION

As a preliminary matter, the *Kelly* test is the logical approach to analyzing the discharge of civil restitution because the Supreme Court has held, and other courts agree, that section 523(a)(7) can apply to civil as well as criminal restitution.¹³⁴ Given that the Supreme Court provided a clear reading of section 523(a)(7) that is consistent with that statute's purpose and legislative history, it makes sense to continue to rely on that interpretation so long as it is effective. As discussed *infra*, the *Kelly* test provides a superior approach to analyzing civil restitution than the alternatives do and would have provided sensible results if applied in *Towers* and *Cost Control Mktg. and Sales Mgmt. of Va.*

B. THE *KELLY* TEST AVOIDS PROBLEMS WITH THE *CCMV* AND *TOWERS* APPROACHES

1. Cost Control Mktg. and Sales Mgmt. of Va.

The primary problem with the *Cost Control Mktg. & Sales Mgmt. of Va.* approach is its lack of analysis regarding the purpose of the restitution in question. That case deemed all restitution that is "penal in nature" to satisfy section 523(a)(7), without requiring a careful look at the penalty or its creation. This approach can result in an overly broad application of section 523(a)(7) and may create problems of statutory construction as well.

One consequence of exempting all restitution that is "penal in nature" is that doing so may protect debts that should be discharged. In *Kelly*, the Supreme Court noted that the purpose of the "for the benefit of a governmental unit" language is to prevent § 523(a)(7) from protecting all "fines, penalties and forfeitures." "It seems likely that the limitation of § 523(a)(7) to fines assessed 'for the benefit of a governmental unit' was intended to prevent

134. See *supra* notes 81, 82, and 85.

application of that subsection to wholly private penalties”¹³⁵ This makes sense because any forced payment of money may be considered a “fine” or “penalty,” but bankruptcy does not protect all debts from discharge. On the contrary, it generally frees debtors from obligations to compensate private parties. Allowing § 523(a)(7) to exempt all “penalties” or debts that are “penal in nature,” as the Fourth Circuit suggests, would lead even private debts to be exempt. Since courts consider all restitution to be “penal,” the approach would protect a civil restitution award from discharge even where a court created it solely for the private purpose of forcing one individual to compensate another. Because payment is penal, it would make no difference that Congress intended to exclude that kind of restitution from exemption. The *Kelly* test avoids the over-inclusion of private debts by applying further analysis to determine the actual purpose of the debt and to decide whether it turns primarily on the penal interests of the government or on the compensatory concerns of the victim. If the debt is private, it fails the test. If it serves to benefit the government’s interests in law enforcement, it merits protection.

In addition to resulting in an overly broad exemption of civil restitution penalties, reading § 523(a)(7) to exempt all debts that are “penal in nature” creates redundancy in the statute. If all “fines, penalties, and forfeitures” operate “for the benefit of the government” because they are “penal in nature,” the “for the benefit” language serves no purpose within § 523(a)(7). Rather, a court must only determine whether a debt is a “fine, penalty, or forfeiture” that does not compensate the government for its pecuniary loss and the analysis is complete. The *Kelly* test avoids this problem as well, providing “fine, penalty or forfeiture” and “for the benefit of the government” with two distinct meanings. The first is easily satisfied by any forced payment of money. The second is only satisfied if the primary purpose of enforcing that payment is to promote the government’s penal interests.

Arguably, the *Kelly* test is also susceptible to criticisms of statutory construction. In fact, that test seems to merge “for the benefit of the government” and “not compensation for actual pecuniary loss” into the same inquiry. Instead of asking (1) if the debt is payable for the benefit of the government, and then (2) if

135. *Kelly v. Robinson*, 479 U.S. 36, 51 n.13 (1986).

it is compensation for pecuniary loss, the *Kelly* test treats the “benefit” and “compensation” prongs in the alternative. However, even if the *Kelly* test renders some phrasing within § 523(a)(7) surplusage, the problem likely is not as serious as it is with *Cost Control Mktg. & Sales Mgmt. of Va.* For one, the *Kelly* test reading of the statute does not also create either an overly broad application of § 523(a)(7) or an unnecessarily narrow one. On the contrary, it seems to comport with Congress’ intent in including the “for the benefit” language by seeking to distinguish between debts that “benefit the government” and debts that are “wholly private” or “compensatory.” Moreover, the *Kelly* test may be susceptible to a minor modification should courts seek to give each prong of § 523(a)(7) a specific purpose and meaning. Although the Supreme Court did not expressly read the statute in this way, both the Fourth and Seventh Circuits construed *Kelly* to deem the “not compensation” element to refer to the *government’s* pecuniary loss. Under this reading, the *Kelly* test could be phrased as three questions: (1) Is the restitution a fine, penalty or forfeiture? (2) Does it operate primarily to benefit the government’s interests in law enforcement or, instead, to compensate victims for harm sustained? (3) Even if the debt primarily serves the government’s law enforcement interests because it mostly considers the situation of the defendant or seeks to punish wrongdoing, will it have the effect of compensating the government for pecuniary loss, as where, e.g., the government will use that restitution to pay for trial costs?

2. Towers

The Seventh Circuit’s approach to exempting civil restitution under § 523(a)(7) is more problematic than the Fourth Circuit’s. The Seventh Circuit’s refusal to accept non-pecuniary benefits to the government can lead to many problems, including (1) requiring an awkward reading of the statute, (2) ignoring the importance of non-pecuniary benefits to the government, (3) requiring reliance on a largely meaningless administrative technicality to distinguish among debts, and (4) relying on inadequate exemption provisions and a flawed cost-benefit analysis to justify all of the above.

a. Awkward Reading

The Fourth Circuit's approach to § 523(a)(7) caused problems of surplusage, *inter alia*, within the statute. The Seventh Circuit's approach also is problematic in terms of statutory construction. For one, the Seventh Circuit's reading seems to create its own redundancies within that provision. Further, the *Towers* understanding of the provision seems incongruous with its language and underlying purpose.

A key problem with the Seventh Circuit's approach to § 523(a)(7) is that it reads the provision to imply the word "pecuniary" because of other language in the statute. The *Towers* court concluded that § 523(a)(7) could only refer to pecuniary benefits because it read the phrase "payable . . . for the benefit of a governmental unit" to imply that the government's "benefit" must be payment of the money itself.¹³⁶ A problem with this reading, however, is that it assumes § 523(a)(7) should imply the term "pecuniary" where it is absent — *i.e.* before "benefit" — even though Congress seems to have added that term in places where it intended to invoke monetary purposes. In the clause subsequent to the "for the benefit" language, the statute does not simply exclude debts that are "compensation for actual loss." Rather, it expressly excludes debts that are "compensation for actual *pecuniary* loss."

Another way of looking at this problem is that reliance on the Seventh Circuit's inference may make part of § 523(a)(7) redundant. If the term "payable" implies "pecuniary" into everything that can be paid, then the reference to payment on debts that might be "compensation for actual pecuniary loss" is partially surplusage. Under this reading, Congress accomplished nothing by specifying that compensation paid to the government is only excluded from § 523(a)(7) if it is for "pecuniary" loss.

A second problem with the Seventh Circuit's interpretation of § 523(a)(7) is that it seems incongruous with the language and purpose of the statute. By reading that provision to protect only penalties that provide pecuniary benefits to the government, the Seventh Circuit focused the § 523(a)(7) inquiry on whether the government would be able to keep the money it receives. This

136. *In re Towers*, 162 F.3d 952, 955–56 (7th Cir. 1998).

approach seems inconsistent with the rest of the language of the statute because it focuses on the government's ability to collect money when the rest of the provision does the opposite. According to the Seventh Circuit, the "for the benefit" language ensures that restitution that might provide a pecuniary benefit to the government is not discharged since penalties created for that reason fall within § 523(a)(7). However, the next line in the statute discharges any debt payable, as the Seventh Circuit agrees, for the *government's pecuniary* loss. Why should the "for the benefit" language work to protect monies paid to the government when the rest of the statute clearly forgives debts that might be payable to the government? If the government's monetary concerns drive the § 523(a)(7) analysis, why should a debt be exempt from discharge where it will provide the government with money and yet be fully dischargeable should it provide the government with reimbursement for money lost?¹³⁷

The seeming incongruity between the Seventh Circuit's reading of "benefits" and "not compensation" may best be understood in terms of the likely purpose of § 523(a)(7). A broader problem with the *Towers* reading is that it treats the statute as if its purpose is to protect debts that might provide money to the government (although not debts that compensate the government), but to discharge debts that do not. It seems highly unlikely, however, that Congress enacted § 523(a)(7) to ensure that the government could fill its coffers. On the contrary, the legislative history provides, and the Supreme Court agrees, that § 523(a)(7) exists to exempt debts that concern effective law enforcement. As noted in *Kelly*, Congress codified that provision against a judicially adopted exception to discharge that existed because courts refused to discharge debts in a way that would thwart law enforcement purposes, not because they or Congress believed the government lost too much money due to over-generous fresh starts. Even leaving legislative history aside, this perspective makes sense. Presumably, Congress would have written a very different statute if it primarily intended to protect the government's ability

137. One way to distinguish between debts payable to provide money to the government and debts payable to reimburse the government for its pecuniary loss is that the former may serve some other purpose, such as to promote compliance with state laws. *Towers*, however, refused to recognize such exterior benefits — to the Seventh Circuit only pecuniary benefits matter.

to collect money from debtors. At the very least, it would have excluded the “not compensation for actual pecuniary loss” language.

b. Ignores the Importance of Non-Pecuniary Benefits

Beyond providing an awkward and problematic reading of § 523(a)(7), the *Towers* approach is flawed because it ignores the importance of non-pecuniary benefits to the government. As discussed above, restitution provides critical benefits to law enforcement that the Supreme Court deemed to drive the “benefits” analysis under § 523(a)(7). Ignoring these benefits is problematic because it may hinder law enforcement by denying effective deterrence, rehabilitation, and punishment that might otherwise flow from protecting civil restitution penalties. The approach also highlights a practical problem with the Seventh Circuit’s reading of § 523(a)(7). If only pecuniary benefits matter, courts must find a way of determining whether they will actually accrue to the government or be disbursed to victims. In *Towers*, the court eventually based its decision on what it thought would happen to the restitution if exempted from discharge. After determining that the Attorney General seemed to have no choice but to disburse money to victims or, if he had any discretion at all, that he certainly *would* pass restitution to victims, the court decided that no monetary benefit would be had and the restitution was dischargeable. The court’s reliance on this administrative technicality — whether the Attorney General intended to or was obligated to disburse payment to victims — is problematic not only because it ignores non-pecuniary benefits, but also because it creates a largely meaningless distinction among civil restitution debts and causes trouble for the government.

The first problem with deciding whether or not to exempt civil restitution debts from discharge based on whether or not the government is obligated to disburse payment to victims is that the distinction seems to have little meaning. As a preliminary matter, the Seventh Circuit acknowledged that the distinction can be made solely based on the technical administration of restitution and without regard to its purpose or even to its eventual recipient. Where the government is required to pass all restitution onto victims, as the court suggested was the case in *Towers*, the government receives no pecuniary benefit according to that court.

Yet, the government *is* deemed to receive a financial benefit under *Towers* when it collects restitution, places it into a general treasury, and then pays the exact amount out to victims. “If an agency collects money and deposits it into the state’s . . . treasury, the fact that the government has a policy of compensating victims of crimes and civil wrongs does not make the collection less ‘for the benefit’ of the government.”¹³⁸ As a result, *Towers* would distinguish between virtually identical debts — neither of which provides any net pecuniary benefit to the government — based solely on the path of payment of the restitution.

Moreover, meaningfully analyzing restitution based on the extent of the government’s discretion in disbursing it can be a difficult proposition. Whereas one court might decline to require a specific disbursement from the government because it intends the restitution solely to benefit the government’s penal interests, another court might grant the government full discretion regarding a debt intended solely to compensate victims because the government has assured the court that it will pass all recovery to those parties or because the government is better suited to handling a proper distribution. The *Towers* holding would exempt both of these debts from discharge even though the first is “penal in nature,” the second may be “wholly private,” and neither would necessarily provide a pecuniary benefit to the government.

Finally, were it somehow meaningful to distinguish between restitution debts that the government is required to pass on and debts that the government can disburse at its choosing, even the Seventh Circuit could not hold to this distinction. Rather, in ruling that the government received no pecuniary benefit from the restitution in *Towers*, the court acknowledged that the Attorney General probably had no obligation to pass the money through to victims, but then set the point aside entirely. Turning away from the government’s *obligation* to disburse, which might be reasonably determinable, the court looked to the government’s purported intent: “[T]he judge did not state in so many words that the Attorney General must redistribute to the victims whatever can be squeezed out of *Towers*. No one doubts, however, that the Attorney General *will* distribute the money to the victims.”¹³⁹ The

138. *Towers*, 162 F.3d at 955.

139. *Id.*

Seventh Circuit held that it could decide whether or not a lower court's ordering of restitution was payable "for the benefit of the government" based solely on the stated plans of the Attorney General, taking the fate of restitution out of the hands of the legislature and the trial court and placing it solely within the power of the prosecuting attorney and the ability of the court to predict her actions.

Ironically, and despite seeming to provide state attorneys with plenary power regarding the disposition of civil restitution penalties, the Seventh Circuit's reading of § 523(a)(7) may also cause real problems for government. Perhaps the biggest pitfall in the Seventh Circuit's reliance on the administration of restitution debts is that it prevents the state from reaping all of the possible benefits associated with restitution. As discussed, *supra*, restitution can be beneficial in terms of deterring misconduct and rehabilitating offenders, but also may be helpful by providing justice to victims, healing harm done, and allowing the offender to provide recompense for her misdeeds. Under *Towers*, these benefits may not co-exist; the government must either (1) refuse to pass money onto victims in order to protect the restitution from discharge and any benefits, such as deterrence or rehabilitation, that might flow from its enforcement, or (2) suggest that it will spend some money to compensate victims so as to reserve the right to accrue other benefits, while risking that the defendant will be able to escape the debt entirely through discharge. *Towers* thus negates the unique effectiveness of restitution, forcing the government to choose between treating those obligations like traditional fines that go solely to the government or like wholly private penalties that compensate victims.

*c. Ignoring Non-Pecuniary Benefits Justified by
Reliance on Inadequate Exemption Provisions and
Flawed Analysis*

The Seventh Circuit's refusal to acknowledge non-monetary benefits for the purposes of § 523(a)(7) is also problematic because the court justified the approach by relying on other exemptions within the Bankruptcy Code and by arguing that non-monetary benefits, such as deterrence, are *costly* to the government. As the Supreme Court noted, the alternative provisions that the court would rely upon to exempt restitution debts are inadequate to

protect the government's interests in all cases. Moreover, a review of the court's analysis of non-pecuniary benefits provided by restitution obligations suggests that its reasoning was misguided.

i. *Reliance on Inadequate Provisions*

The Seventh Circuit recognized that its reading of § 523(a)(7) could operate against the government's penal interests in some cases. The court nevertheless declined to change its analysis because it believed the government could rely on other sections of the Bankruptcy Code to protect benefits such as deterrence. "If there were no way to protect the deterrence effects of restitution except by hammering away at 'for the benefit of' until it fit the mold, then a court might be tempted. But it is not necessary [because other provisions provide that protection]."¹⁴⁰

The Seventh Circuit was correct that the government could have avoided the discharge of restitution in *Towers* by objecting under other provisions of the Bankruptcy Code in *Towers*'s bankruptcy and that the government may be able to rely on these provisions in many cases. However, the court likely was wrong that a broader understanding of § 523(a)(7) would never be necessary to protect the government's interests. In *Kelly*, the Supreme Court expressly rejected the argument for a narrow reading of § 523(a)(7) that the Seventh Circuit employed in *Towers*. As in *Towers*, the government could have objected to Robinson's debt in her earlier bankruptcy case under other exemption provisions of the Bankruptcy Code; because her crime involved larceny and fraud, either § 523(a)(2) or § 523(a)(4) would have sufficed had the government raised its objections sooner. The Court declined to punish the government for its inaction, however, because "reliance on a right to appear and object to discharge would create uncertainties and impose undue burdens on state officials".¹⁴¹

In many cases, of course, principles of issue preclusion would obviate the need for the bankruptcy court to reexamine factual questions, or interpret state law. But differences between the elements of crimes and the provisions of § 523

140. *Towers*, 162 F.3d at 956.

141. *Kelly*, 479 U.S. at 48.

frequently might hinder the application of issue preclusion. Moreover . . . some restitution orders would not be protected from discharge even if the State did appear and enter an objection to discharge.¹⁴²

The concerns raised in *Kelly* are equally relevant to the enforcement of *civil* restitution obligations. First, forcing the government to object under other provisions can impose undue burdens. In fraud cases, for example, the government could object under § 523(a)(4), but while some federal courts require a showing of common law fraud, state courts do not.¹⁴³ As a result, the government objecting under § 534(a)(4) might have to offer greater proof in bankruptcy court than it did to obtain the original penalty. Second, as with criminal restitution, the alternative methods of avoiding discharge will not always be available to the government for protecting civil restitution penalties. For example, “the Code does not expressly designate consumer fraud . . . as nondischargeable,”¹⁴⁴ leaving § 523(a)(7) as the only option for exempting restitution arising from such misconduct.¹⁴⁵

ii. *Justified by Flawed Analysis of Non-Pecuniary Benefits*

The Seventh Circuit’s reading of the “for the benefit of a governmental unit” language is also problematic because it seems to rely on a flawed analysis of non-pecuniary benefits. The court concluded that non-pecuniary benefits such as “deterrence” could not satisfy the “for the benefit of the government” language because they actually are “costly” to the government — “the ‘governmental unit’ does not receive any benefit from general deter-

142. *Id.* at 48 n.8.

143. S. REP. NO. 100-119, at 9 (1987), *reprinted in* 1988 U.S.C.C.A.N. 683, 691. (“There is more to this ‘loophole’ in our law enforcement. At least one U.S. Court of Appeals has held that the State Attorney General lacked standing to challenge the dischargeability of a consumer protection restitution order he has obtained.”).

144. *Id.*, *reprinted in* 1988 U.S.C.C.A.N. 683, 690-91.

145. *Id.* (“First, there is litigation in State court under the consumer protection statutes. Second, after judgment or default, defendants frequently seek haven in bankruptcy court to avoid repayment of ill-gotten gains. Many of these defendants succeed because the Code does not expressly designate consumer fraud or any other type of civil restitution orders as non-dischargeable.”).

rence either.”¹⁴⁶ This analysis is susceptible to a number of criticisms. First, the *Towers* argument assumes that the government willingly acts against its own interests. In some cases, such as *Cost Control Mktg. & Sales Mgmt. of Va.*, the government has no obligation to pass restitution onto victims, but may want to do so anyway. According to the Seventh Circuit, this must be irrational since doing it is doubly costly: the government is hurt by both the outlay and the resulting deterrence. Rather than substitute the court’s analysis for the state’s in such cases, it may be more reasonable to assume that the government has reasons for what it does. The government may seek to enforce civil restitution, for example, because it derives benefits from that effort even, and perhaps especially, when it passes payment on the debt to victims.

Second, even following the Seventh Circuit’s “public choice” approach to government benefits, it is not clear that the “cost” of pursuing deterrence and passing money onto victims would actually be higher than the costs associated with *foregoing* those benefits. Whatever short-term perks additional money might provide to a given governmental unit, enforcing the law less effectively in order to garner more funding likely is not a viable long-term strategy. Presumably, the public will eventually punish governmental units charged with law enforcement — either through ouster or budget cuts — if those bodies continue to reject opportunities to promote compliance with state laws. Almost certainly, political opponents of those in office will take the opportunity to highlight such policy gaffes.

Finally, the Seventh Circuit’s approach seems to deny that the government benefits from a job well done. By assuming that the government only benefits from money retained, the court ignores that governmental units exist to serve the public, not simply to line their coffers.

C. THE *KELLY* TEST PROVIDES SENSIBLE RESULTS WHERE OTHER APPROACHES MAY NOT

A final reason courts should apply the *Kelly* test to civil restitution penalties is that it provides sensible results on facts where

146. *In re Towers*, 162 F.3d 952, 956 (7th Cir. 1998).

other approaches may not. Specifically, the *Kelly* test probably would have yielded more satisfying results if applied to the facts of *Cost Control Mktg. & Sales Mgmt. of Va.* and *Towers*.

1. Cost Control Mktg. & Sales Mgmt. of Va.

Stepping away from the legal intricacies of the case, the holding in *Cost Control Mktg. & Sales Mgmt. of Va.* is generally satisfying. Whatever the shortcomings of that case's analysis, it seems right that four officers of a company that defrauded home buyers of millions of dollars should not escape their duty to pay restitution simply by filing for bankruptcy. What justice is there if bankruptcy provides a haven for wrongdoers in this way? The only issue tempering this conclusion is the concern of the unknown.

As discussed, the problem with the Fourth Circuit's approach is that it did not delve deeply into the nature and purpose of the restitution at issue.¹⁴⁷ Instead, after finding it to be "penal," the court held the penalty in place.¹⁴⁸ Facially, this seems a fair result, but what if the court looked to the statute giving rise to the restitution and to the judgment order creating it and found that the CCMV officers were already punished for their wrongdoing? What if, for example, the trial court required each officer to pay fines and penalties far in excess of their profits and of the damage done to victims and then also required them to pay restitution solely to compensate victims for their losses? In such a case, the result in *Cost Control Mktg. & Sales Mgmt. of Va.* might seem less palatable; rather than holding the defendants responsible for their debts to society, the exemption would serve primarily to damage any hope they might have of a "fresh start" and would do so for a solely private, compensatory purpose.

Applied to the facts in *Cost Control Mktg. & Sales Mgmt. of Va.*, the *Kelly* test would have asked two questions to determine whether or not the restitution in question operated primarily to benefit the government's penal interests or, instead, to compensate victims. First: Did the victims exercise significant control over the awarding or amount of the restitution? The answer to

147. See *supra* Part III.B.

148. *U.S. HUD v. Cost Control Mktg. & Sales Mgmt. of Va., Inc.*, 64 F.3d 920, 928 (4th Cir. 1995).

this question would almost certainly have been “no.” The CCMV officers’ victims were Virginia home-buyers and the Department of Housing and Urban Development brought the suit giving rise to the restitution. At most, the actual victims of the fraud in *Cost Control Mktg. & Sales Mgmt. of Va.* could have influenced the restitution as witnesses.

The second question the *Kelly* test would have asked is whether the statute and judgment order giving rise to the restitution primarily turn on concerns of the victim (rather than on the situation of the defendant or the penal interests of the government). Also consistent with the result in *Cost Control Mktg. & Sales Mgmt. of Va.*, the answer to this question likely would have been “no.” For one, the decision resulting in the restitution seemed to focus on the situation of the defendants, specifically seeking to estimate the amount of “ill-gotten profits” received from the enterprise and taking into consideration that the defendants “contumaciously refused to disclose evidence that would have provided a better foundation” for the court’s order of restitution.¹⁴⁹ Rather than looking to the amount each victim lost and seeking to provide the appropriate reimbursement, “the district court doubtless envisioned that a searching inquiry into the individual defendants’ finances would follow to see how much of the ill-gotten gains had flowed through CCMV and into their pockets.”¹⁵⁰ Moreover, the discussion of civil penalties potentially awarded under the Interstate Land Sales Full Disclosure Act strongly suggests that the statute focuses on both the situation of the defendant and the state’s interests in effective law enforcement. Section 1717(b), “Civil Penalties,” provides in pertinent part:

(3) Factors in determining amount of penalty: In determining the amount of a penalty under subsection (a) of this section, consideration shall be given to such factors as the gravity of the offense, *any history of prior offenses* (including offenses occurring before December 15, 1989), *ability to pay the penalty, injury to the public, benefits received, deterrence*

149. *Id.* at 926–27.

150. *Id.* at 926.

of future violations, and such other factors as the Secretary may determine in regulations to be appropriate.¹⁵¹

The statute's focus on prior offenses, ability to pay the penalty, and the potential for deterring future violations, suggests that it primarily concerns the government and the defendant, rather than the need to compensate victims.

2. Towers

Unlike the result in *Cost Control Mktg. & Sales Mgmt. of Va.*, the conclusion of the *Towers* court is not particularly satisfying. Rather than holding Towers responsible for the money he cheated from homeowners by offering them hope, the Seventh Circuit upheld Towers's fresh start. Ironically, the court seemed to do so because Towers's victims might receive some recompense for the harm done to them and even though providing such compensation could be consistent with effective law enforcement. Applying the *Kelly* test to the facts of that case suggests that the court need not have arrived at this unfortunate outcome, even if it chose to look solely to the law and away from unpleasant facts.

Applied to the facts in *Towers*, the *Kelly* test would have provided the opposite result — holding Towers responsible for his restitution debts. The restitution in question would easily have passed the first prong of that test since the Illinois Attorney General and not Towers's victims brought the suit, requested the restitution, and received it upon court order. Looking to the statute giving rise to that restitution suggests that the Towers's debt likely would have passed the second prong of the *Kelly* analysis as well. That obligation arose under the Illinois Consumer Fraud and Deceptive Business Practices Act.¹⁵² That statute is clear in expressing that penalties created pursuant to its provisions are “designed to protect the public interest” rather than to compensate victims.¹⁵³ As held in *Scott v. Association for Childbirth at Home, Int'l*,¹⁵⁴ the act is “clearly within the class of remedial statutes which are designed to grant remedies for the protection of

151. 15 U.S.C. 1717(b) (emphasis added).

152. 815 ILL. COMP. STAT. 505/7 (2000).

153. *People ex rel. Ryan v. Towers (In re Towers)*, 217 B.R. 1008 (N.D. Ill. 1998).

154. 430 N.E.2d 1012 (Ill. 1981).

rights, introduce regulation conducive to the public good, or cure public evils.”¹⁵⁵ In fact, it expressly restricts suits for penalties and restitution brought under its auspices to situations where “proceedings would be in the public interest.”

V. CONCLUSION

In conclusion, courts should apply the Supreme Court’s approach to criminal restitution obligations when deciding whether to exempt civil restitution from discharge under § 523(a)(7) of the Bankruptcy Code. In addition to being as applicable to civil restitution debts as it is to criminal restitution obligations, the *Kelly* test avoids many of the problems associated with other approaches employed in the civil context and is likely to provide sensible and satisfying results on facts where those approaches might not.

155. *Id.* at 1017.