

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF NEW YORK

IN RE:

RICHARD H. CONZ

CASE NO. 97-60429

Debtor

Chapter 7

JAMES C. COLLINS, Trustee

Plaintiff

vs.

ADV. PRO. NO. 99-80017A

RICHARD H. CONZ, JOHN J. BROMINSKI
and THE CHASE MANHATTAN BANK

Defendants

APPEARANCES:

JAMES C. COLLINS, ESQ.
Attorney for Plaintiff/Trustee
P.O. Box 713
Whitney Point, New York 13862-0713

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Attorney for Richard H. Conz
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Hon. Stephen D. Gerling, Chief U.S. Bankruptcy Judge

**MEMORANDUM-DECISION, FINDINGS OF FACT,
CONCLUSIONS OF LAW AND ORDER**

Currently before the Court is an adversary proceeding commenced on January 21, 1999, by the chapter 7 trustee, James C. Collins ("Trustee"), seeking revocation of the discharge of Richard H. Conz ("Debtor") pursuant to §§ 727(d) of the Bankruptcy Code, 11 U.S.C. §§ 101-

1330 (“Code”).¹ Issue was joined by the filing of an answer by the Debtor on May 3, 1999.

After at least two adjournments on consent of the parties, a trial was held on March 15, 2000, in Utica, New York. In lieu of closing arguments, the Court requested that the parties file memoranda of law by April 14, 2000. The matter was submitted for decision on that date.

JURISDICTIONAL STATEMENT

The Court has core jurisdiction over the parties and subject matter of this adversary proceeding pursuant to 28 U.S.C. §§ 1334, 157(a), 157(b)(1) and (2)(A) and (J).

FACTS

The Debtor filed a voluntary petition (“Petition”) pursuant to chapter 7 of the Code on January 29, 1997. The Debtor received a discharge on June 6, 1997. Listed in the Debtor’s schedules was a 24’ pontoon boat and trailer (“Boat”) valued at \$8,200. *See* Plaintiff’s Exhibit 4. Chase Manhattan Bank (“Chase”) was listed as a secured creditor with a security interest in the Boat. *See id.* According to the Debtor’s Statement of Intention, he planned to retain the Boat and reaffirm the debt owing to Chase. *Id.* Also listed in the Debtor’s schedules was a purchase and sale agreement (“Purchase Agreement”) for the sale of the Debtor’s liquor business to John J. Brominski (“Brominski”) on May 2, 1996. *Id.* Brominski testified that he paid the Debtor

¹ Although the Trustee’s complaint included causes of action against two other defendants, those matters were resolved prior to trial.

approximately \$15,000 at the time of the sale and under the terms of the Purchase Agreement he was to pay the balance of between \$7,000 and \$8,000 in monthly installments of \$250. According to the Debtor, he used approximately \$12,000 of the proceeds to pay off liquor distributors because of his concerns that they would refuse to deliver liquor to the new owner, except on a “cash on delivery” basis. These payments apparently were made before he filed his Petition.

Debtor listed the monthly installments from Brominski as income in Schedule I. *See id.* The Debtor testified that he used those monies to make his monthly payments of \$290 to Chase on the Boat. The payments to Chase were identified in Schedule J as a monthly expense of the Debtor. *Id.*

The meeting of creditors pursuant to Code § 341 was held on March 17, 1997. *See* Defendant’s Exhibit C. In response to an oral request made by the Trustee at that meeting, on March 18, 1997, Debtor’s counsel forwarded to the Trustee a copy of the Purchase Agreement and a copy of the certificate of title for the Boat, along with a statement from Chase regarding its lien on the Boat. *See* Defendant’s Exhibits A and B. On or about June 22, 1998, the Trustee wrote Debtor’s counsel requesting a copy of his federal and state tax returns for the years 1995-1997, a copy of the Purchase Agreement, and a list of all monies received by the Debtor in connection with the sale of the liquor business. *See* Defendant’s Exhibit D. The Trustee testified that although this was the first time he had communicated with Debtor’s counsel in writing since the meeting of creditors, he had communicated by telephone with counsel sometime in 1997 requesting those items. However, he did not have his telephone log with him in court to substantiate when such conversation had occurred.

The Trustee acknowledged on direct examination that in March 1997 he received a letter

from Debtor's counsel, which, *inter alia*, included a copy of the Purchase Agreement. He was also aware that the Debtor had listed the \$250 monthly payments as income in his schedules, as well as the fact that he was making payments to Chase of \$290 per month.

On August 21, 1998, the Trustee obtained an Order requiring that the Debtor provide him with an accounting of the monies received pursuant to the Purchase Agreement and also requiring that he turnover any monies received from the petition date in connection with the Purchase Agreement to the Trustee. *See* Plaintiff's Exhibit 2. The Debtor was also required to provide the Trustee with a copy of Chase's security agreement, as well as proof of Chase's perfection of a security interest in the Boat. *See id.* The Debtor testified that he did not remember receiving the Order, but he did recall his attorney mentioning it to him. He also acknowledged that in August 1998 he was using the Boat. It was his testimony that the Boat was later placed into storage as he had paid for storage for the season, but that he knew that eventually someone would be taking the Boat. The Trustee acknowledged that he had received \$1,000 in payments from Brominski via the Debtor's attorney and had also recovered the Boat, which he later sold.

DISCUSSION

The relevant portion of Code § 727(d) provides that, upon the trustee's request, a court shall revoke a debtor's discharge if any of three grounds set out in the statute is established upon notice and a hearing. *See* 11 U.S.C. § 727(d). The two proffered justifications for the revocation of the discharge in this case are that (1) "the debtor acquired property that is property of the estate, or became entitled to acquire property that would be property of the estate, and knowingly

and fraudulently failed to report the acquisition of or entitlement to such property, or to deliver or surrender such property to the trustee;” and/or (2) “the debtor committed an act specified in subsection (a)(6) of this section.” *See* 11 U.S.C. § 727(d)(2), and (d)(3). Subsection (a)(6) of Code § 727 lists, among others, a refusal on the part of the debtor to obey a court order. *See* 11 U.S.C. § 727(a)(6)(A).

“As the revocation of a debtor’s discharge is a harsh measure and runs contrary to the general bankruptcy policy of giving Chapter 7 debtors a ‘fresh start,’ a bankruptcy court should only do so for reasons clearly expressed by a statute.” *In re Magack*, 247 B.R. 406, 409 (Bankr. N.D. Ohio 1999) (citations omitted). Additionally, a request to revoke a debtor’s discharge under Code § 727(d)(2), and (d)(3) must be made either within one year of the granting of the discharge, or before the case is closed. *See* 11 U.S.C. § 727(e)(2).²

“[R]evocation is an extraordinary remedy.” *In re Weisberg*, 202 B.R. 332, 334 (Bankr. D. N.H. 1996) (citations omitted). The burden of proof is on the plaintiff in an action for revocation of a discharge. *See Matter of Yonikus*, 974 F.2d 901, 904 (7th Cir. 1992). Courts are split as to whether the burden of proof to meet Code § 727 criteria merely requires a preponderance of the evidence standard or the more difficult clear and convincing standard. The majority of courts require only a preponderance of the evidence standard. *See In re Reese*, 203 B.R. 425, 430 (Bankr. N.D. Ill. 1997) (citations omitted); *In re Sylvia*, 214 B.R. 437, 440 (Bankr. D.Conn. 1997) (citations omitted); *In re Constantini*, 201 B.R. 312, 315 (Bankr. M.D. Fla. 1996) (citations omitted). Once the plaintiff produces enough evidence to sustain his or her burden, the

² The Trustee in this case commenced the adversary proceeding more than a year after the Debtor received his discharge but prior to the close of the case.

burden then shifts to the defendant to explain his or her actions. *See id.* Furthermore, Code § 727 is to be liberally construed in the debtor's favor. *See In re Vereen*, 219 B.R. 691, 694 (Bankr. D.S.C. 1997); *Weisberg*, 202 B.R. at 334 (citation omitted).

Code § 727(d)(2) Claim

Under Code § 727(d)(2), a trustee can move to have a debtor's discharge revoked if the debtor obtained property that is property of the estate, and "knowingly and fraudulently" neglected to reveal or transfer this asset to the trustee.

[T]he Bankruptcy Rules clearly indicate that one of the duties of the debtor is to cooperate with the trustee in the administration of estate. Fed. R. Bankr. P. 4002(4). Furthermore, courts addressing other subsections of Section 727 conclude that a debtor is under an affirmative duty to cooperate with the trustee by providing all requested information, and that failure to comply constitutes grounds for denial of discharge [citations omitted] * * *. A debtor seeking the benefit of a discharge pays a price. That price is the performance of certain duties, such as cooperation with the Trustee.

Reese, 203 B.R. at 431-32.

"To find the requisite degree of fraudulent intent, the court must find the debtor knowingly intended to defraud the trustee, or engaged in such reckless behavior as to justify the finding of fraud." *Yonikus*, 974 F.2d at 905. Evidence of fraud can include deliberate omissions, failure to report important information, or "a pattern of fraudulent deception." *Id.* at 906. A court may infer fraudulent intent from the conduct of the debtor, or from the surrounding circumstances. *Id.* at 905-6 (citations omitted). "Under Section 727(d)(2), no requirement of lack of knowledge is expressly provided in the statute, but courts have interpreted the language to require the trustee

learn of the fraud after the discharge was granted.” *Reese*, 203 B.R. at 430-31; *Vereen*, 219 B.R. at 694; *In re Lyons*, 23 B.R. 123, 126 (Bankr. E.D. Va. 1982). In addition, courts have said that if the plaintiff possesses the information when an objection can be raised prior to a discharge, and does not act on it, the plaintiff cannot later seek a revocation of that discharge pursuant to Code § 727(d)(2). *Vereen*, 219 B.R. at 695, citing *In re Richard*, 165 B.R. 642, 643 (Bankr. W.D. Ark. 1994); *Lyons*, 23 B.R. at 126. The plaintiff in an action for revocation of a discharge has an “affirmative duty” to investigate any possible fraud before the discharge is given, when the possibility of fraud is reasonably suspected. *Id.*, citing *In re Cochard*, 177 B.R. 639 (Bankr. E.D. Mo. 1995). Further, a trustee must demonstrate “proper diligence in attempting to discover the necessary facts before the discharge.” *Vereen*, 219 B.R. at 695, citing *In re Benak*, 91 B.R. 1008, 1009-10 (Bankr. S.D. Fla. 1988).

Code § 521(1) requires that the Debtor file a schedule of assets and liabilities. *See In re Kottmeier*, 240 B.R. 440, 442 (M.D. Fla. 1999). Code § 521(4) also requires that the Debtor “surrender to the Trustee all property of the estate and any recorded information, including books, documents, records and papers related to property of the estate.” 11 U.S.C. § 521(4). This has been interpreted to mean that “a constructive delivery is made at the time the case is filed [by listing the assets in the debtor’s schedules’] and physical delivery can be made, where suitable, on the trustee’s request.” *In re Figueira*, 163 B.R. 192, 194 (Bankr. D.Kan. 1993). The court in *Figueira* pointed out that debtors should not have to collect all debts owed to them and then surrender the monies to the trustee. *Id.* The court noted that the debtors were merely obliged to make the information available to the trustee. *Id.*

In *In re Sylvia*, 214 B.R. 437 (Bankr. D. Conn. 1997), the court revoked the debtors’

discharge under Code § 727(d)(2), finding that the debtors acted fraudulently in that they knew certain monies were property of the estate, and failed to inform the trustee of their receipt of the funds and failed to turn them over to the trustee. *See id.* at 441. Conversely, in *Richard*, the court denied the plaintiff's Code § 727(d)(2) claim, stating that there was no evidence that "the debtor failed or refused to turnover property to the trustee, that he acquired an interest in property, or that any such acquisition was unreported." *Richard*, 165 B.R. at 644. The court added that although there were important omissions, the court did not deem them "fraudulent," and the evidence had revealed that the debtor had honestly and openly responded to all questions at the creditors' meeting and had disclosed all the information which the plaintiff claimed the debtor had hidden. *Id.*

While the Trustee here demonstrated that the Debtor retained property that rightfully belonged to the bankruptcy estate, including the Boat and the monies received from Brominski, nothing in the evidence presented at trial supports a finding by the Court that the Debtor's actions were in any way fraudulent or that there was a pattern of deception on his part. Not only had the Debtor revealed the assets in his Petition, he also appears to have openly responded to the Trustee's questions at the meeting of creditors and promptly provided the Trustee with the information requested regarding those assets. The Trustee allowed the discharge to be granted without objection and gave no direction as to the disposition of the Debtor's postpetition assets relating to the sale of his liquor store until almost a year after the Debtor's discharge. Though a Trustee may request the revocation of a discharge until the case is closed, the Trustee here had an obligation to investigate the Debtor's assets and liabilities that were listed in his Petition prior to the granting of his discharge. Absent any proof of fraud, the Court has no basis to revoke the

Debtor's discharge pursuant to Code § 727(d)(2).

Code § 727(d)(3) Claim

Revocation of a debtor's discharge pursuant to Code § 727(d)(3) is discretionary. *See In re Klein*, 1995 WL 656696 (E.D. La. 1995) at *3 (citing *In re Koskoszka*, 479 F.2d 990 (2d Cir. 1973), *aff'd* 417 U.S. 642 (1974)). As the Court of Appeals for the Second Circuit noted, a court "should consider such factors as the intent behind the bankrupt's acts - were they wilful or was there a justifiable excuse; was there injury to the creditors; and is there some way the bankrupt could make amends for his conduct." *Koskoszka* at 998. While a debtor's noncompliance with a court order can warrant the revocation of a discharge, *see Klein*, 1995 WL 656696 at *2 (citation omitted), "mere noncompliance" is insufficient. *See Magack*, 247 B.R. at 409, *citing Constantini*, 201 B.R. at 316. As noted by the court in *In re Jarrell*, 129 B.R. 29 (Bankr. D. Del. 1991),

Section 727(a)(6)(A) allows this court to deny a discharge only if the debtors 'refused' to obey the court order. The use of the word 'refused' in §727(a)(6)(A) must be distinguished from the use of the word 'failed' elsewhere in §727(a). Bankruptcy law recognizes that mere failure does not equal refusal where the creditor does not show wilful or intentional disobedience, as opposed to inability, inadvertence or mistake.

Id. at 33 (citations omitted).

The August 21, 1998 Order required that the Debtor provide an accounting to the Trustee and turnover to him all monies received pursuant to the Purchase Agreement from the date of the Petition going forward. The Debtor was also to provide the Trustee with a copy of the security

agreement with Chase and proof of the bank's perfection of its security interest in the Boat. The Debtor testified that except for the four months of payments paid to the Trustee by Brominski in October 1998, all monies he had received had been paid to Chase in connection with the loan on the Boat. While the Trustee apparently never obtained a copy of the security agreement with Chase from the Debtor, the Debtor had provided him with evidence of Chase's perfection, or lack thereof, of its security interest in March 1997 by furnishing the Trustee with a copy of the certificate of title on the Boat. There is no evidence that the Debtor ever refused to turnover the Boat to the Trustee, and no evidence was offered at the trial to indicate that the Trustee ever obtained an order of the Court in that respect. The Trustee also indicated that he had settled with Chase with respect to the first cause of action in his complaint in which he alleged that Chase had failed to perfect its security interest in the Boat. In addition to seeking to avoid Chase's security interest, the Trustee also sought turnover of all monies received by Chase from the Debtor postpetition pursuant to Code § 549, as well as monies received within ninety days of the Debtor's filing of his Petition pursuant to Code § 547.

The Court is not convinced that the Debtor's actions have been so egregious as to merit the severe remedy of the revocation of his discharge. The Trustee has offered no meaningful evidence to demonstrate that the Debtor's actions, in failing to fully comply with the August 21, 1998 Order, have significantly prejudiced the estate or harmed his creditors. The Trustee has not shown to the Court's satisfaction that the Debtor "refused" to comply with the August 21, 1998 Order for purposes of Code §727(d)(3).

While the Court certainly does not condone the actions of anyone who chooses to ignore its orders, the Court also believes in this situation that the Debtor should not be penalized for the

Trustee's delay in acting on the information contained in the Debtor's schedules and the information provided to the Trustee immediately following the meeting of creditors in March 1997. Had the Trustee sought an order in March 1997, when he first learned of the Purchase Agreement, requiring Brominski to pay him directly, there would have been no need for the Debtor to provide the Trustee with an accounting of the monies received from Brominski postpetition. Once the Trustee received the copy of the certificate of title from the Debtor in March 1997 which he requested, the Trustee certainly was in a position to make inquiry of Chase concerning its alleged security interest in the Boat and to take appropriate actions to avoid the transaction and seek turnover of the Boat. Through no fault of the Debtor and without explanation, the Trustee waited for over a year to act on the information provided to him by the Debtor. Despite the delay, the Trustee was able to recover \$1,000 from Brominski and was able to recover monies from the sale of the Boat for the benefit of the Debtor's unsecured creditors.

Under the circumstances, the Court concludes that the Trustee has failed to establish by a preponderance of the evidence that the Debtor's discharge should be revoked pursuant to Code § 727(d)(3), incorporating by reference Code § 727(a)(6).

Based on the foregoing, it is hereby

ORDERED that the Trustee's complaint seeking revocation of the Debtor's discharge pursuant to Code § 727(d) (2) and (3) is denied and the within adversary proceeding is dismissed.

Dated at Utica, New York

this 4th day of October 2000

STEPHEN D. GERLING
Chief U.S. Bankruptcy Judge