

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF NEW YORK

IN RE:

LEAH DIOLOLA PATTERSON

Debtor

CASE NO. 96-65888

Chapter 7

CAROLYN J. COOLEY, TRUSTEE

Plaintiff

vs.

ADV. PRO. NO. 98-70807A

LEAH DIOLOLA PATTERSON

Defendant

APPEARANCES:

CAROLYN J. COOLEY, ESQ.
Attorney for Plaintiff
Mayro Building, Room 405
Utica, New York 13501

RICHARD E. KAPLAN, ESQ.
Attorney for Defendant
2626 Sunset Avenue
Utica, New York 13502

Hon. Stephen D. Gerling, Chief U.S. Bankruptcy Judge

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

Under consideration by the Court is evidence presented at a trial conducted on January 13, 1999, in Utica, New York, in connection with an adversary proceeding commenced by the chapter 7 trustee, Carolyn J. Cooley, Esq. ("Trustee") on May 26, 1998. The Trustee seeks an order revoking the discharge of Leah Diolola Patterson ("Debtor") pursuant to §§ 727(d) and

727(a)(6)(A) of the Bankruptcy Code (11 U.S.C. §§ 101-1330) (“Code”). Issue was joined by the filing of an Answer on behalf of the Debtor on June 22, 1998.

The trial was originally scheduled to be held on September 16, 1998, and was subsequently adjourned on consent of the parties to November 9, 1998, and finally to January 13, 1999. Following the taking of testimony, the parties were provided with an opportunity to file memoranda of law in lieu of closing arguments. The matter was submitted for decision on February 10, 1999.

JURISDICTIONAL STATEMENT

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

FACTS

The Debtor filed a voluntary petition pursuant to chapter 7 of the Code on December 13, 1996. On January 9, 1997, a meeting of creditors pursuant to Code § 341 (“§ 341 Meeting”) was conducted in Utica, New York. At the § 341 Meeting the Trustee requested that the Debtor provide her with copies of her tax returns for 1995 and 1996. It was the Debtor’s testimony that she informed her husband of the need to file the income tax returns and provide copies to the Trustee, but after reminding him a few times and having him become upset with her, she simply forgot about it.

On or about March 13, 1997, the Trustee sought an ex parte order of the Court directing the Debtor (1) to prepare the 1995 and 1996 Federal and State income tax returns; (2) to immediately forward copies of such returns to the Trustee on the date the returns were forwarded to the taxing authorities, and (3) to immediately endorse any tax refund checks for the years 1995 and 1996 to the Trustee and to deliver them to her forthwith. *See* Trustee's Exhibit 3. An Order was signed on March 14, 1997, granting the Trustee's application ("March 14th Order"). *See id.* The March 14th Order includes a statement advising the Debtor that "failure to comply with the foregoing order is a ground for the denial or revocation of a discharge in bankruptcy." *Id.*

Mr. Patterson, the Debtor's husband, testified that upon receiving a copy of the March 14th Order, he hired someone to file the tax returns for 1995 and 1996, in April 1997. Joint tax returns for both the Debtor and her husband were prepared and filed with the taxing authorities for 1996 on or about April 3, 1997. *See* Debtor's Exhibit D. Joint returns for 1995 were prepared and filed on or about April 10, 1997. *See id.* With respect to both Federal income tax returns, the couple received a refund of approximately \$1,800 for each of the two years and paid the State a total of approximately \$210 in additional tax due for the two years combined. *See id.* Mr. Patterson admitted that he had not forwarded copies of the returns to the Trustee.

Mr. Patterson testified that after his wife filed for bankruptcy in December 1996, he became aware that she had a serious gambling problem. The Debtor's testimony confirmed this. As a result, he took all financial matters away from her. He did not let her see bank statements; he took her paychecks and deposited them into an account in his name after closing out their joint accounts. The only money she was given was for gasoline for her car and for lunches. According to Mr. Patterson, in February 1997, he sought counseling for work-related stress and

depression. He explained that with all that was going on at the time, many things slipped his mind. He also testified that he and his wife received no correspondence from either her attorney or the Trustee in either March or April of 1997 indicating that there was a problem.

On May 26, 1998, the Trustee filed a complaint seeking revocation of the Debtor's discharge.¹ The Debtor, as well as her attorney, were served with the summons and copy of the Trustee's complaint by first class mail on May 28, 1998. Mr. Patterson testified that it was not until he read the Trustee's complaint that he became aware of the fact that the Trustee was seeking to have his wife's discharge revoked based on the Debtor's failure to provide copies of the couple's tax returns to her and her failure to turnover refunds received for 1995 and 1996. It was his testimony that he immediately contacted the Debtor's attorney and was told to send a copy of the returns to the Trustee. In addition to the returns, Mr. Patterson sent the Trustee a check in the amount of \$710.56, representing what he calculated to be the Debtor's prorated share of the refunds based on their respective incomes for 1995 and 1996. The check, however, was returned by the Trustee because, according to Mr. Patterson, the Trustee felt she was entitled to half of the refunds. As a result, he contacted Charles J. Schoff, CPA ("Schoff") to determine "who owned what" with respect to the refunds.

Schoff testified that, in his opinion, the Debtor was not entitled to any part of the Federal tax refunds. He testified that the approximately \$3,600 received in refunds was the result of withholdings from Mr. Patterson's salary. In a letter dated December 14, 1998, and addressed to Mr. Patterson, he stated that "[t]he refunds generated had nothing to do with the tax withheld from your wife's wages only with your excess withholdings." *See* Debtor's Exhibit C. He also

¹ The Debtor had received a discharge on April 7, 1997.

testified that if the Debtor had filed separately, she would have had to pay \$375 and \$417, respectively, for 1995 and 1996, because the withholdings from her salary were inadequate to satisfy her tax liability.

ARGUMENTS

It is the Trustee's position that the Debtor's failure to supply her with copies of the couple's income tax returns pursuant to the Court's March 14th Order is grounds for the revocation of her discharge. The Trustee stresses what she considers to be the Debtor's lack of effort to comply with the provisions of the March 14th Order. The Trustee also makes the argument that "the refunds should be treated as owned jointly by both parties to the return, with one-half being due to the bankruptcy estate." *See* Trustee's Memorandum of Law, filed February 10, 1999.

Debtor's counsel asserts that the Debtor's failure to comply with the terms of the March 14th Order was not intentional. Instead, Debtor's counsel argues that it was through inadvertence or neglect that the Debtor failed to follow through with the mailing of the tax returns to the Trustee. With respect to the turnover of the tax refunds, it is the Debtor's position, based on Schoff's testimony, that she was not entitled to any and, therefore, there is nothing to turn over to the Trustee. Debtor's counsel points out that there have been no allegations that the Debtor's noncompliance with the terms of the March 14th Order was an attempt to defraud her creditors or that the Debtor in any way benefitted from her failure to comply with the March 14th Order.

DISCUSSION

“Revocation of a discharge is a harsh measure and runs contrary to the general policy of the Bankruptcy Code of giving Chapter 7 debtors a ‘fresh start.’” *In re Kaliana*, 202 B.R. 600, 603 (Bankr. N.D. Ill. 1996) (citations omitted). The Trustee has the burden of establishing the elements of Code § 727(d) by a preponderance of the evidence. *See id.* (citing *Grogan v. Garner*, 498 U.S. 279, 286-87, 111 S.Ct. 654, 659-60, 112 L.Ed.2d 755 (1991)). Furthermore, Code § 727(d) is to be construed strictly against the Trustee, as the party seeking revocation of the Debtor’s discharge, and in favor of the Debtor’s retention of her discharge. *See Kaliana*, 202 B.R. at 603 (citations omitted).

It is clear that, with the exception of filing the tax returns for 1995 and 1996, the Debtor failed to comply with the terms of the March 14th Order until after the Trustee commenced this proceeding. The Court certainly does not condone the violation of one of its orders. The Court also recognizes that it is necessary that a chapter 7 trustee have an understanding of a debtor’s status with respect to the taxing authorities if she/he is to properly administer the estate. *See In re Smith*, 1995 WL 241398 at *4 (Bankr. D.Idaho 1995) (noting that “compliance with the court’s orders concerning tax returns and refunds is crucial.”).

Nevertheless, the Second Circuit Court of Appeals, citing to *Pepper v. Litton*, 308 U.S. 295, 305, 60 S.Ct. 238, 244, 84 L.Ed. 281 (1939), has stated that “Bankruptcy Courts must exercise their powers so that ‘substance will not give way to form’ and ‘technical considerations will not prevent substantial justice from being done.’” *In re Kokoszka*, 479 F.2d 990, 997 (2d Cir. 1973), *aff’d* 417 U.S. 642, 94 S.Ct. 2431, 41 L.Ed.2d 374 (1974). The Second Circuit noted that

[t]he denial of a discharge can work a serious deprivation upon a debtor, and there are many circumstances where a bankrupt's disobedience may have been inadvertent or otherwise excusable. * * * Therefore, . . . [the court] should weigh the detriment to the proceedings and the dignity of the court against the potential harm to the debtor if the discharge is denied. [It] 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 that the bankrupt could make amends for his conduct.

Id. at 997-98.²

Code § 727(d)(3), read in conjunction with Code § 727(a)(6)(A), requires that the Court revoke a debtor's discharge if the debtor refused, in the case, to obey any lawful order of the court, other than an order to respond to a material question or to testify. In this case, there is no evidence that the Debtor *refused* to obey the Court's March 14th Order. Based on her testimony, it is clear that she had to rely on her husband to file the returns given his decision to handle all financial matters of the couple in an effort to remedy the situation with respect to her gambling problem. The Court finds Mr. Patterson's testimony to the effect that in early 1997 he was overwhelmed with the situation in which he found himself credible. He testified that he was receiving treatment for work-related stress and depression. In addition, he chose to lend support to his wife in her effort to recover from her gambling addiction. He apparently was not involved in the Debtor's decision to file bankruptcy and was not aware of the importance of providing the Trustee with copies of the tax returns until he read the Trustee's complaint. At that point, he immediately contacted Debtor's counsel and on his advice forwarded copies of the tax returns

² The Second Circuit's determination in *Kokoszka* was rendered pursuant to the Bankruptcy Act of 1898. However, because the language of Code § 727(a)(6)(A) is the same as that found in § 47(c)(6)(A) of the Bankruptcy Act, cases interpreting the latter section are relevant to the matter now before this Court under the Code. *See In re Costantini*, 201 B.R. 312, 315 n.2 (Bankr. M.D.Fla. 1996).

to the Trustee, along with what he estimated to be the Debtor's prorated share of the refunds.

As noted above, Code § 727(a)(6)(A) requires that a debtor *refuse* to obey a court order for there to be a basis for revocation of the debtor's discharge. Mere "failure" to obey the order is not sufficient. *See Costantini*, 201 B.R. at 316, citing *In re Jarrell*, 129 B.R. 29, 33 (Bankr. D.Del. 1991). It is necessary that the Trustee establish that the Debtor wilfully and intentionally disobeyed the March 14th Order. *See id.* No such showing was made at the trial. In addition, there was no evidence of any injury to creditors as a result of the delay in providing the Trustee with copies of the Debtor's tax returns. *See Commerce Bank & Trust Co. v. Burgess (In re Burgess)*, 955 F.2d 134, 138 (1st Cir. 1992), citing to *Kokoszka*.

With respect to the refunds, the Trustee offered no evidence to counter Schoff's testimony that the Debtor was not entitled to any of the refunds. Under the circumstances, the Court finds no merit to the Trustee's assertion that the estate is entitled to half of the refunds because the couple filed a joint return. As Schoff testified, had the Debtor filed a separate Federal return, she would have owed money to the government. Therefore, there were no refunds to turn over to the Trustee.

Based on the evidence presented, the Court finds that the Trustee has failed to meet her burden of proof under Code §§ 727(d) and 727(a)(6)(A).

Based on the foregoing, it is hereby

ORDERED that the Trustee's complaint seeking revocation of the Debtor's discharge is dismissed.

Dated at Utica, New York

this 25th day of February 1999

STEPHEN D. GERLING
Chief U.S. Bankruptcy Judge