

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF NEW YORK

IN RE:

ROBERT D. REESE
SHAWN S. REESE

Debtors

CASE NO. 97-61903

Chapter 13

DARRYL CROSS

Plaintiff

vs.

ADV. PRO. NO. 01-80066A

ROBERT D. REESE and MARK W.
SWIMELAR, in his official capacity
as Chapter 13 Trustee

Defendants

APPEARANCES:

MARK W. SWIMELAR
Chapter 13 Trustee/Defendant
250 South Clinton St., 5th Floor
Syracuse, New York 13202

LYNN HARPER WILSON, ESQ.
Of Counsel

RICHARD P. RUSWICK, ESQ.
Attorney for Debtors
P.O. Box 6693
Ithaca, New York 14851-6693

THE CROSSMORE LAW OFFICE
Attorneys for Plaintiff
115 West Green Street
Ithaca, New York 14850

EDWARD Y. CROSSMORE, ESQ.
Of Counsel

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 the cross-motion filed by Robert D. Reese (“Debtor”) on February 7, 2002, seeking to dismiss certain causes of action asserted in an adversary proceeding commenced by Darryl Cross (“Cross”) on May 23, 2001.¹

Oral argument was heard at the Court’s regular motion term in Binghamton, New York, on April 9, 2002. The Court determined that Cross’ second cause of action in his complaint, asserting that certain funds allegedly held by the Debtor constituted cash collateral, had no basis as a matter of law and dismissed it. The Court reserved its decision on whether 28 U.S.C. § 959, which served as the basis for Cross’ first cause of action, is applicable to a chapter 13 debtor and allows a party to commence a lawsuit based on Article 3-A of the New York Lien Law (“NYLL”).

Cross then filed a motion by Order to Show Cause on May 7, 2002, seeking approval of the payment of an administrative claim pursuant to Code § 503(b).² An objection was filed by the Debtors, Robert and Shawn Reese, on May 13, 2002.

¹ On January 30, 2002, Cross filed a motion seeking to amend his complaint to add a cause of action based on § 503(b) of the Bankruptcy Code, 11 U.S.C. §§ 101-1330 (“Code”), and to add the chapter 13 trustee, Mark W. Swimelar, Esq. (“Trustee”), as a defendant. Following a hearing on March 19, 2002, the Court signed an Order on March 28, 2002, granting the motion. The Court adjourned Debtor’s cross-motion, which was filed in response to Cross’ motion, to April 9, 2002.

² Cross’ attorney, Edward Y. Crossmore, Esq. (“Crossmore”), acknowledged to the Court that the relief requested was the same as what had been requested in the fourth cause of action in Cross’ amended complaint, filed on April 5, 2002. He explained that the Trustee had requested that the relief sought be filed as a motion so that the Trustee would not need to notify his insurance carrier that a lawsuit had been commenced against him. On May 30, 2002, the Trustee filed a motion in the adversary proceeding requesting an extension of time to answer the amended complaint. The Court signed a Consent Order on June 12, 2002, granting the extension while the matters addressed herein were pending.

The motion was heard on May 14, 2002, at the Court's regular motion term in Binghamton, New York. Following oral argument, the Court determined that it would be necessary to hold an evidentiary hearing to address whether Cross was entitled to an administrative claim and whether laches prevented him from recovering on such a claim.³

An evidentiary hearing was held on June 24, 2002, in Utica, New York. Following testimony by both the Debtor and Cross, the Court provided both parties with an opportunity to file memoranda of law. The matter was submitted for decision on July 31, 2002.

JURISDICTIONAL STATEMENT

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

FACTS

The Debtors filed a voluntary petition pursuant to chapter 13 of the Code on April 2, 1997. Their chapter 13 plan was confirmed on October 15, 1997, and provided for payments over five years.

According to the testimony of Cross, he was hired by the Debtor, d/b/a Fall Creek

³ The Court also adjourned Trustee's motion, filed on April 25, 2002, seeking approval of the disbursement of funds in his possession in connection with the Debtors' case and the filing of a Final Report and Account, to June 24, 2002, the date of the evidentiary hearing.

Homes,⁴ in May 1999 to do certain excavation and grading work at a building site on Briar Meadows Road, Town of Homer, New York (hereinafter referred to as the “McAvoy job”). Cross testified that he began the work on June 4, 1999 and completed it on October 10, 1999. *See* Cross’ Exhibits C and D. According to Cross, he was paid \$6,000 by the Debtor, leaving a balance of \$6,075.⁵

Cross testified that at the time he was hired by the Debtor as a subcontractor on the McAvoy job, he was unaware that the Debtor was in bankruptcy. He first learned of the bankruptcy filing when he received a letter, dated March 22, 2001, from Debtor’s counsel, Richard P. Ruswick, Esq. *See* Cross’ Exhibit E. The letter apprized Cross that he could file a post-petition claim in the case and receive payments from the Trustee, but that he was precluded from taking any action to collect the debt pursuant to Code § 362. *See id.* It was Cross’ testimony that upon receipt of the letter he contacted his attorney who referred him to Crossmore.

The Debtor testified that he had underbid the McAvoy job by approximately \$6,000. He testified that he had paid Cross \$6,000 and did not dispute that he owed Cross approximately \$7,000 more in connection with his work on the McAvoy job. *See also* Movant’s Exhibit K, at 6. The Debtor also testified that Cross had done an excellent job in performing the work.

According to the business ledger prepared by the Debtor in 1999, on or about May 7, 1999, he was paid \$8,000 in connection with the McAvoy job. *See* Cross’ Exhibit L. A second

⁴ At the time the Debtors filed their petition, Mr. Reese was doing business as Reese Construction. He testified that he changed the name of his company to Fall Creek Homes postpetition to reflect a change in the type of work he was doing.

⁵ Cross testified that there were additional “items not priced” totaling \$1,600 for which he also billed the Debtor. *See* Cross’ Exhibit D.

payment was received on or about June 14, 1999, in the amount of \$14,000, and a third payment on or about July 23, 1999, in the amount of \$40,860. *Id.* He received an additional payment on or about September 7, 1999, in the amount of \$38,100 and a final payment of \$23,000 on or about October 15, 1999, for a total of \$123,960 paid to the Debtor in connection with the McAvoy job. *Id.* According to the ledger, a check in the amount of \$6,000 was issued to Cross on or about August 3, 1999.

The Debtor testified that the McAvoy job was completed in December 1999. According to the Debtor, it was the last job he did as an independent contractor until January 2002. Beginning in February 2000 he worked for a commercial construction company in Syracuse, New York, until July 2001.

Debtor's wife was also employed at the time that they filed their petition. According to the Debtors' schedules she had worked for the Department of Motor Vehicles for ten years. Debtor testified that the monies paid to the Trustee came from income she earned. It was his testimony that the monies did not come out of the business checking account. However, he also testified that his accountant had had him list the monthly payments of \$600 to the Trustee as a business expense under the heading "Materials" because most of the debt identified in his schedules was business related.⁶ *See id.*

Cross' complaint, as amended and filed on April 5, 2002 ("Amended Complaint"), sets forth four causes of action against Debtor Robert Reese. The first cause of action is based on Article 3-A of New York Lien Law. Cross alleges that the Debtor, as contractor, had certain

⁶ The Debtor's ledger for 1999 identifies \$136,494.86 in income and \$139,463.39 in expenses, including the payments to the Trustee. *Id.*

fiduciary duties with respect to monies paid to him by the owner of the house, Donald McAvoy (“McAvoy”), for which Cross provided excavation and grading services. Cross contends that pursuant to 28 U.S.C. § 959 he is entitled to sue the Debtor to recover \$7,657 allegedly owed him without seeking permission from this Court.

As previously noted, at the hearing on April 9, 2002, the Court dismissed Cross’ second cause of action which asserted that the monies received by the Debtor from McAvoy constituted cash collateral within the meaning of Code 363(a).

Cross’ third cause of action asserts that the Debtor should be required to account for his activities as a debtor engaged in business under Code § 1304 and should be subject to surcharge for any violation of such duties. Finally, Cross asserts in his fourth cause of action an entitlement to an administrative expense claim pursuant to Code § 503.

DISCUSSION

Applicability of 28 U.S.C. § 959 to a Chapter 13 Debtor

At least one court has examined the applicability of 28 U.S.C. § 959 to a chapter 13 debtor and concluded that it does not have application because a chapter 13 debtor in whom property of the estate is usually revested is neither a debtor-in-possession nor a trustee. *See In re Robertson*, 2000 WL 33716977 at *2 (Bankr. D.Or.). However, it is also true that the commencement of a judicial proceeding against a chapter 13 debtor based on a claim which arose after the commencement of the case is not stayed pursuant to Code § 362(a). *See In re York*, 13 B.R. 757, 758 (Bankr. D. Maine 1981); *see also Bellini Imports, Ltd. v. Mason and Dixon Lines*,

Inc., 944 F.2d 199, 201 (4th Cir. 1991) (noting that “[t]he stay is limited to actions that could have been instituted before the petition was filed or that are based on claims that arose before the petition was filed. (citation omitted). It does not include actions arising post-petition.”); *Turner Broadcasting System, Inc. v. Sanyo Elec., Inc.*, 33 B.R. 996, 1000 (N.D. Ga. 1983), *aff’d*, 742 F.2d 1465 (11th Cir. 1984) (indicating that “the stay is not designed to be an offensive weapon - a sword - which would permit the debtor to benefit unilaterally from the breaching of a post-bankruptcy petition contract that he voluntarily entered into.”). However, “a creditor must obtain relief from the automatic stay to satisfy a judgment against property of the bankruptcy estate.” *Bellini Imports*, 944 F.2d at 201. Accordingly, Cross is not precluded from suing the Debtor postpetition to recover what he asserts are trust funds and not property of the estate. He would not be able to satisfy any judgment, however, until either he obtained relief from the automatic stay or waited until the Debtor’s discharge is granted.

The fact that Cross may sue the Debtor postpetition does not mean that he may sue the Debtor in this Court to recover what he alleges are trust funds pursuant to Article 3-A of the NYLL. This is particularly true when one considers the fact that under New York law, Cross had a year from the date on which final payment under his contract with the Debtor became due or from the date of completion of the improvement, whichever was later, to enforce any trust arising under Article 3-A. *See* NYLL § 77(2) (McKinney 1993 & Supp. 2002); *In re Tripp*, 189 B.R. 29, 34 (Bankr. N.D.N.Y. 1995); *In re Grosso*, 9 B.R. 815, 822 (Bankr. N.D.N.Y. 1981).

Cross testified that he was hired in May 1999 to work on the McAvoy job. It was his testimony that he completed the work in October 1999. According to the invoice submitted by Cross to the Debtor and dated October 5, 1999, payment from the Debtor was to be made within

30 days. *See* Cross' Exhibit D. The Debtor testified that the McAvoy job was completed the latter part of December 1999. Therefore, the statute of limitations is to be measured from sometime in the latter part of December 1999. Cross commenced the adversary proceeding by filing his complaint on May 23, 2001, approximately seventeen months after completion of the improvement. Having this Court adjudicate the matter would constitute an impermissible circumvention of the state statute on which he is basing his demand and under which he is time barred from seeking relief in state court. Therefore, the Court will dismiss Cross' first cause of action on the basis that it is barred by the statute of limitations set forth in NYLL § 77(2).

Entitlement to an Administrative Expense pursuant to Code § 503(b)

Cross has asserted a claim for an administrative expense both by motion and in the Fourth Cause of action of his Amended Complaint. Code § 503(b) refers to the allowance of administrative expenses which include “the actual, necessary costs and expenses of preserving the estate. Code § 503(b) is made applicable to the Debtor's case by Code § 364(a), which provides that if the trustee/debtor is authorized to operate a business under Code § 1304, he/she may incur unsecured debt in the ordinary course of business “allowable under 503(b)(1) of this title as an administrative expense.”

The Court has broad discretion in determining whether to award administrative expense priority, and the allowance of an administrative expense is to be narrowly construed. *See In re Molnar Bros.*, 200 B.R. 558-59 (Bankr. D. N.J. 1996). In this case, Cross argues that his services were rendered in connection with the ordinary course of the Debtor's construction business. He contends that the services preserved the value of the Debtor's business as a going

concern and allowed the Debtor to generate income from which to pay his creditors. As a claimant seeking priority status, Cross has the burden of proof. *See id.; In re ICS Cybernetics, Inc.*, 111 B.R. 32, 37 (Bankr. N.D.N.Y. 1989) (citation omitted).

To sustain that burden, he had to establish by a preponderance of the evidence that his claim (1) arose out of a postpetition transaction with the Debtor and (2) provided a direct benefit to the estate. *See Molnar Bros.*, 200 B.R. at 559. (citations omitted) (emphasis added). The fact that the claim arose postpetition in the ordinary course of the Debtor's business is not sufficient in and of itself to warrant priority status. It is also necessary that Cross establish that services were "actual" and "necessary" and benefitted the estate as a whole. *Id.*

The Debtor testified that the McAvoy job, which was completed in December 1999, was the last one he performed as an independent contractor until January 2002. Debtor testified further that he actually had underbid the McAvoy job, taking a loss of approximately \$6,000. Furthermore, upon completion of the McAvoy job, he ceased doing business as an independent contractor and was employed by a commercial construction company for approximately eighteen months, between February 2000 and July 2001. There was no testimony offered by Cross to contradict Debtor's testimony. Based on the evidence presented, the Court concludes that Cross' services, and the debt which was incurred by the Debtor in connection with those services, did not preserve the value of the Debtor's business as a going concern and are not entitled to be paid as an administrative expense as having benefitted the estate. Accordingly, Cross' motion, as well as the fourth cause of action in his Amended Complaint, based on Code § 503(b) is denied.⁷

⁷ Based on the Court's conclusions herein, it is unnecessary that the Court address the applicability of the doctrine of laches to the facts of this case.

Third Cause of Action alleging Breach of Fiduciary Duty

Cross' third cause of action in his Amended Complaint alleges that the Debtor breached his fiduciary duty as a debtor engaged in business under Code § 1304. Cross contends that the Debtor should be required to account for his activities and be subject to a surcharge for any breach of that duty. Courts have on occasion noted that a debtor has a fiduciary duty to prepetition creditors. *See, e.g. In re Lively*, 266 B.R. 209, 217 (Bankr. N.D. Okla. 1998) (noting debtors' fiduciary duty to treat general unsecured creditors the same in making a distribution to them); *In re Tornheim*, 181 B.R. 161, 169 (Bankr. S.D.N.Y. 1995), *appeal dismissed*, 1996 WL 79333 (S.D.N.Y.) (indicating that debtors have a fiduciary duty to provide financial disclosure to their creditors). However, in this case, Cross is not a creditor of the estate and, therefore, he has no standing to assert a breach of any such duty, even if one were to exist. Therefore, the Court will dismiss Cross' third cause of action.

Motion Seeking Approval of the Disbursement of Funds and Filing of a Final Account

At the hearing on May 14, 2002, it was represented to the Court that the Trustee was holding approximately \$2,400 for disbursement to creditors pursuant to the terms of the Debtors' chapter 13 plan. Based on the findings herein, the Court will grant the Trustee's motion to disburse the remaining funds and file a final account.

Code § 1328(a) requires the Court to grant the Debtors a discharge upon completion of their payments under the plan. Pursuant to Code § 1328(a), the discharge does not apply to the debt at issue. Therefore, Cross may pursue whatever remedies he might have available in state court to collect the debt.

Based on the foregoing, it is hereby

ORDERED that Cross' motion seeking an administrative expense claim pursuant to Code § 503(b) is denied; it is further

ORDERED that the Debtor's motion seeking dismissal of the Amended Complaint is granted; and it is finally

ORDERED that the Trustee's motion seeking approval of the disbursement of funds and the filing of a final account is granted.

Dated at Utica, New York

this 28th day of October 2002

STEPHEN D. GERLING
Chief U.S. Bankruptcy Judge