UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF NEW YORK

IN RE:

JAMES JAY BALL — CASE NO. 02-60810

Debtor — Chapter 7

A.O. SMITH CORPORATION

Plaintiff

vs. — ADV. PRO. NO. 02-80127

JAMES JAY BALL

Defendant

APPEARANCES:

LEONARD, STREET AND DENARD
Attorneys for Plaintiff
150 South Fifth Street, Suite 2300
Minneapolis, Minnesota 55402

FREDERICK W. MORRIS, ESQ.
Of Counsel
JEFFREY A. EYRES, ESQ.
Of Counsel

JAMES JAY BALL, ESQ.
Attorney for Defendant
Box 22, Rt. 28
Meridale, NY 13806

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

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

Presently under consideration is an adversary proceeding commenced by the filing of a complaint on June 4, 2002, by A.O. Smith Corporation ("Plaintiff" or "AOS"). Plaintiff seeks a determination of nondischargeability of a debt owed by James J. Ball ("Debtor") pursuant to § 523(a)(6) of the U.S. Bankruptcy Code, 11 U.S.C. §§ 101-1330 ("Code"). Issue was joined by

the filing of an answer by the Debtor on July 8, 2002.

The trial was originally scheduled for September 23, 2002, and was adjourned to December 16, 2002, on consent of the parties. It was subsequently adjourned to March 13, 2003, in order to allow the parties an opportunity to resolve certain discovery issues. On March 14, 2003, the Court issued a Scheduling Order, setting a deadline for discovery of June 2, 2003, and scheduling the trial for July 17, 2003.

The trial was held on July 17, 2003, in Utica, New York. The Court declined to allow the testimony of Plaintiff's counsel, Frederick Morris, Esq. ("Morris") and Jeffrey Eyres, Esq. ("Eyres"), upon the request of the Debtor that they be stricken as witnesses on behalf of the Plaintiff because of the inherent conflict of representing the Plaintiff while acting as a witness on Plaintiff's behalf. Debtor based his request on Disciplinary Rule 5-102(A) which provides that

> A lawyer shall not act, or accept employment that contemplates the lawyer's acting, as an advocate on issues of fact before any tribunal if the lawyer knows or it is obvious that the lawyer ought to be called as a witness on a significant issue on behalf of the client . . . .

22 N.Y.C.R.R.[1] § 1200.21.

Over the objection of the Debtor, the Court allowed the admission of the transcript ("Tr.") of a three day proceeding held before the Hon. Tucker L. Melancon ("Judge Melancon"), of the U.S. District Court for the Western District of Louisiana ("District Court"). *See* Plaintiff's Exhibit 3.[2] The Court reserved on the admission of the transcripts of hearings held before the

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[1] Codes, Rules & Regulations of the State of New York.

[2] The transcript consists of two days of testimony and oral argument on January 29-30, 2001, followed by the issuance of oral rulings by Judge Melancon on January 31, 2001 ("January

District Court on September 3, 1999 and November 3, 1999. *See* Plaintiff's Exhibits 9 and 10. There was no testimony presented by either party.

The Court requested that the parties submit post-trial memoranda of law by August 29, 2003, with the understanding that the parties would be permitted an extension if the transcript of the trial was unavailable. Accordingly, the parties were granted an extension until September 23, 2003. By letter, dated September 23, 2003, Debtor requested a further extension because he had not, as of that date, received the transcript.[3] The Court agreed to extend the deadline until no later than October 30, 2003.

By letter, dated October 24, 2003, Debtor requested that the Court enforce the disciplinary rules by ordering that Morris and Eyres withdraw from the case. The Court responded to the Debtor's request on October 27, 2003, informing the Debtor that the Court was unable to grant relief requested in letter form and that the Debtor should consider filing a motion. By Order to Show Cause, filed October 28, 2003, Debtor sought an order revoking the *pro hac vice* admission of Morris and Eyres. According to the Debtor, in conducting research in preparation for submitting his post-trial memorandum of law, he discovered that the rules were mandatory and required that attorneys who violated them withdraw from employment. He argued that in declining to allow the testimony of Morris and Eyres at the trial on July 17, 2003, the Court had concluded that they had violated the disciplinary rules.

At a hearing held on November 20, 2003, in connection with the Order to Show Cause,

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2001 Rulings").

[3] According to the Bankruptcy Court Clerk's office, Debtor had not requested a copy of the transcript until September 15, 2003, and had not requested it on an expedited basis. Therefore, he would not receive it until October 15, 2003.

the Court admonished the Debtor that it perceived the request to be yet another attempt on his part to delay the submission of his post-trial memorandum and denied the relief sought.[4] The Court ordered the Debtor to file his memorandum of law on or before December 10, 2003. The Court also allowed the Plaintiff until December 30, 2003, to file its response. The matter was taken under submission on December 30, 2003.

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), (b)(1) and (b)(2)(I) and (O).

FACTS

The following facts emerge from the record of the proceedings held in the District Court on January 29-31, 2001 (*see* Plaintiff's Exhibit 3):

In 1977 Timothy Gautreau and his brother, Steven, purchased a used silo manufactured by the Plaintiff. On or about June 29, 1998, a lawsuit was commenced in the District Court, captioned Timothy Gautreau, *et al.* v. A.O. Smith Corporation, *et al.*. Debtor represented the Gautreaus in the lawsuit. At some point in the proceedings, AOS filed a motion for summary judgment, alleging that "the plaintiffs' state law fraud claims and the federal RICO claims were barred by prescription and the statute of limitations, respectively." *See* January 2001 Rulings at

[4] Plaintiff had submitted its post-trial memorandum of law on October 29, 2003, in compliance with the extension granted by the Court to both parties.

4-5. The District Court granted the motion and dismissed the action with prejudice. *Id.* at 5.

On or about October 29, 1999, AOS filed a motion with the District Court pursuant to Rule 11 of the Federal Rules of Civil Procedure ("Fed.R.Civ.P.") and pursuant to 28 U.S.C. § 1927. *See* Tr. of 1/29/2001 at 75-76. The basis for the Rule 11 motion, as alleged by AOS, was that the Debtor had

> violated Rule 11 by presenting plaintiff's complaint for an improper purpose to harass and to cause unnecessary and needless litigation expense; that the complaint was not warranted by existing law or by a non-frivolous argument for the extension, modification or reversible [*sic*] of existing law or the establishment of new law; and that allegations and other factual contentions contained within the complaint lacked evidentiary support even after a reasonable opportunity for investigation and discovery.

January 2001 Rulings at 6-7.

Judge Melancon heard testimony on the motion from the Debtor, as well as Timothy Gautreau, on January 29-30, 2001. The main focus of the hearing, according to Judge Melancon, was on the issue of "whether [the case] should have been filed in the first place from the get-go, not about what happened after I did what I did on September 3rd dismissing the individual defendants, not about the hearing that I had on November 3rd." *See* Tr. of 1/29/2001 at 71. "The issue is what did you [the Debtor] have that gave you a reason to believe that you could file this suit, that it was timely, had merit." *Id.* at 104.

At the hearing, Morris asserted that there "was not a reasonable inquiry of the facts, or if there was a reasonable inquiry of the facts, that there was not a reasonable inquiry into the law to see whether, based on those facts, there was a colorable claim that could be made." Tr. of 1/30/2001 at 9. At the end of the two days of hearings, Judge Melancon concluded that "[t]here was not a colorable claim when the lawsuit was filed. *See* January 2001 Rulings at 10.

He also found that "it was unreasonable to bring the suit in the first place . . . ." *Id.* at 11 and 12. Judge Melancon found it unnecessary to award sanctions based on the court's inherent power but noted that based on the record before him, he "would be within the bounds set for the use of the court's inherent power to impose a sanction." *Id.* at 15. Instead, he based his award of sanctions against the Debtor, which included shifting the entire financial burden of defending the action to the Debtor, on Rule 11 and 28 U.S.C. § 1927. *Id.* at 13-14.

On or about March 27, 2002, the Court of Appeals for the Fifth Circuit affirmed the District Court's imposition of monetary sanctions against the Debtor of $168,397.21. *See* Debtor's Exhibit N. In the interim, on February 13, 2002, the Debtor filed a voluntary petition pursuant to chapter 7 of the Code. Plaintiff is listed as an unsecured creditor with a claim of $168,397.21, plus interest, "pursuant to Order of the U.S. District Court, Western District of Louisiana," dated June 18, 2001. *See* Schedule F of the Debtor's Petition. Also listed was a claim of the Plaintiff for $1,669.79 in attorney's fees in connection with an application allegedly made by AOS on January 31, 2002 in the District Court. *Id.*

DISCUSSION

Plaintiff has the burden of establishing the elements of Code § 523(a)(6) by a preponderance of the evidence. *See Grogan v. Garner*, 498 U.S. 279, 285 (1991). Plaintiff must prove that the Debtor's actions in commencing the lawsuit in the District Court was "a deliberate or intentional act that leads to injury." *Kawaauhau v. Geiger*, 523 U.S. 57, 61 (1998). Plaintiff must also establish that the Debtor's actions were "malicious." This requires that the Plaintiff demonstrate that the Debtor's conduct was wrongful and undertaken without just cause or excuse.

In re Chaires, 249 B.R. 101, 104 (Bankr. D.Md. 2000) (citation omitted); *In re Slosberg*, 225 B.R. 9, 21 (Bankr. D.Me. 1998); *In re Carlson*, 224 B.R. 659, 662 (Bankr. N.D. Ill. 1998), *aff'd French Keseli & Kominiarek, P.C. v. Carlson (In re Carlson)*, No. 99 C 6020, 2000 WL 226706 (N.D. Ill. Feb. 22, 2000), *aff'd* 2001 WL 1313652 (7th Cir. Oct. 23, 2001); *see also In re Mitchell*, 227 B.R. 45, 51 (Bankr. S.D.N.Y. 1998) (noting that malice "can be implied when anyone of reasonable intelligence knows that the act in question is contrary to commonly accepted duties in the ordinary relationship among people, and injurious to another"). There need not be proof that the Debtor's actions were motivated by ill-will or spite. *See Navistar Financial Corp. v. Stelluti (In re Stelluti)*, 94 F.3d 84, 87 (2d Cir. 1996).

In meeting its burden of proof, Plaintiff offered no admissible testimony at the trial. Instead, it offered in evidence a copy of the transcript of the two days of hearings before Judge Melancon, as well as the transcript of the January 2001 Rulings. *See* Plaintiff's Exhibit 3. This Court's use of the transcripts for purposes of its inquiry concerning whether Debtor's actions were willful and malicious under Code § 523(a)(6) requires the Court to examine whether the doctrine of collateral estoppel applies.

"In the nondischargeability context, where a court rules against the debtor upon specific issues of fact that independently comprise elements of a dischargeability claim, collateral estoppel precludes the debtor from relitigating those underlying facts in bankruptcy court." *Carlson*, No. 99 C 6020, 2000 WL 226706, at *4; *see also Grogan*, 498 U.S. at 284 n.11 (stating that "collateral estoppel principles do indeed apply in discharge exception proceedings pursuant to § 523(a)"). Whether to apply collateral estoppel to Judge Melancon's rulings in this case depends on whether the Debtor had a fair and full opportunity to litigate the issues and whether the requisite elements of Code § 523 (a)(6) were specifically decided by the District Court. *See*

In re Halperin, 215 B.R. 321, 336 (Bankr. E.D.N.Y. 1997). In this regard, the record in the District Court must sufficiently "'reveal the controlling facts and pinpoint the exact issues litigated in the prior action.'" *Id.*, quoting *In re Tobman*, 107 B.R. 20, 23 (Bankr. S.D.N.Y. 1989).

The January 2001 Rulings were issued following two days of testimony and argument, including that of the Debtor. In awarding sanctions against the Debtor, Judge Melancon expressly found that there was not a colorable claim when the lawsuit was commenced (January 2001 Rulings at 10), and it was unreasonable for the Debtor to have brought the lawsuit. *Id.* at 11 and 12. He concluded that the Debtor had violated Rule 11, as well as 28 U.S.C. § 1927.

Under Rule 11, sanctions can be imposed only if the Debtor's position could "'fairly be said to be unreasonable from the point of view of both existing law and its possible extension, modification or reversal.'" *FDIC v. Calhoun*, 34 F.3d 1291, 1296 (5th Cir. 1994), quoting *Smith v. Our Lady of the Lake Hosp., Inc.*, 901 F.2d 439, 444 (5th Cir. 1992). In this case, Judge Melancon made an expressed finding

> that the prescription issue as to the state law claim which plaintiff's attorney later withdrew in his opposition to defendant's summary judgment and the statute of limitations issue as to the RICO claim were so obviously abar [*sic*] that under the circumstances it was unreasonable to bring the suit in the first place . . . .

January 2001 Rulings at 11.

Judge Melancon's acknowledged that 28 U.S.C. § 1927 "is to be sparingly applied, and except when the entire course of the proceedings were unwarranted and should neither have been commenced nor persisted in, an award under 28 U.S.C. § 1927 may not shift the entire financial burden of an action's defense." *Id.* at 9 and 13-14. The Fifth Circuit Court of Appeals made a

specific finding that the District Court had given "sufficient reasons for the sanctions award, including the type and amount of the sanctions." *Ball v. A.O. Smith Corp.,* No. 01-30336 (5th Cir. March 27, 2002).

In order to have awarded sanctions pursuant to 28 U.S.C. § 1927, it was implicit that Judge Melancon found that the Debtor's actions, not only unreasonable, but also "vexatious" and in bad faith or undertaken for an improper purpose.[5] *See Travelers Ins. Co. v. St. Jude Hosp. of Kenner, LA, Inc.*, 38 F.3d 1414, 1416-17 (5th Cir. 1994); *see also Moore v. Western Sur. Co.*, 140 F.R.D. 340, 349 (N.D. Miss. 1991), *aff'd* 977 F.2d 578 (5th Cir. 1992) (stating that "an award of attorney's fees under Section 1927 'must be of an egregious nature, stamped by bad faith that is violative of recognized standards in the conduct of litigation'" (citation omitted)).

Under the law of the Fifth Circuit, in order to have affirmed the District Court's award of sanctions under both Rule 11 and 28 U.S.C. § 1927, these reasons had to have included the finding that the commencement of the lawsuit against AOS by the Debtor was unreasonable, vexatious or in bad faith. "Acts that are in bad faith, vexatious, wanton and for oppressive reasons, are acts that are an intentional injury, without cause or excuse, and are thus both 'willful' and 'malicious' for purposes of 11 U.S.C. § 523(a)(6)." *Chaires*, 249 B.R. at 106 (citations omitted); *In re Huber*, 171 B.R. 740, 747-754 (Bankr. W.D.N.Y. 1994). Under the circumstances, the Court concludes that the doctrine of collateral estoppel is applicable to this proceeding. The transcripts of the two days of hearing in January 2001, as well as the January 2001 Rulings, sufficiently establish that the motion against the Debtor for sanctions was fairly

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[5] "Vexatious" is defined as lacking justification and intended to harass. WEBSTER'S THIRD NEW INTERNATIONAL DICTIONARY 248 (1981). "Bad faith" is defined as "dishonesty of belief or purpose." BLACK'S LAW DICTIONARY 134 (7th ed. 1999).

and fully adjudicated and that Judge Melancon made specific findings in support of the Court's conclusions that the Debtor's actions in commencing the lawsuit in District Court were willful and malicious, causing injury to AOS in the form of costs and attorney's fees in having to defend the lawsuit. Accordingly, the Court concludes that Plaintiff has met its burden by a preponderance of the evidence.[6]

Based on the foregoing, it is hereby

ORDERED that the debt owed to Plaintiff in the amount of $168,397.21, as awarded by the District Court on June 18, 2001, is nondischargeable pursuant to Code § 523(a)(6).

Dated at Utica, New York

this 10th day of February 2004

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STEPHEN D. GERLING
Chief U.S. Bankruptcy Judge

[6] The Court will deny the admission of Plaintiff's Exhibits 9 and 10 on the basis of relevancy. The District Court made it clear in its January 2001 Rulings that it deemed it important that the Fifth Circuit Court of Appeals have available to it the transcripts of the prior proceedings in the District Court, held on September 3, 1999 and November 3, 1999. Given the Fifth Circuit's affirmation of Judge Melancon's rulings, this Court does not believe it necessary to consider them in reaching its conclusions.