UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF NEW YORK

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IN RE:

WILLIAM C. BRITTON — CASE NO. 02-64030

Debtor — Chapter 7

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APPEARANCES:

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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 a motion ("Debtor's Motion") filed on October 1, 2003, by William C. Britton, d/b/a K-9 Cleaners ("Debtor"), seeking an order vacating, in part, an Order of this Court, dated September 22, 2003, pursuant to Rule 60(b) of the Federal Rules of Civil Procedure ("Fed.R.Civ.P."), as incorporated in Rule 9024 of the Federal Rules of Bankruptcy Procedure ("Fed.R.Bankr.P."). Opposition to the Debtor's Motion was filed on October 29, 2003, on behalf of 1105-1141 Broadway Corporation ("Landlord").

The Debtor's Motion was originally heard on November 4, 2003, at the Court's regular motion term in Syracuse, New York. Following oral argument, the Court adjourned the Debtor's

Motion to allow the parties an opportunity to distinguish the holding in *In re Babbs*, 265 B.R. 35 (Bankr. S.D.N.Y. 2001). Following oral argument on December 2, 2003, the Court agreed to take the matter under submission for decision.

## JURISDICTIONAL STATEMENT

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

## FACTS

The Debtor filed a voluntary petition pursuant to chapter 13 of the Bankruptcy Code,11 U.S.C. §§ 101-1330 ("Code"), on July 2, 2002. According to the Debtor's Statement of Financial Affairs, at the time of filing he operated a dog grooming business at 628 S. Main Street, North Syracuse, New York 13212 (the "Premises"). The Debtor leased the Premises from The Peter Family Irrevocable Trust, allegedly the Landlord's predecessor-in-interest. *See* Landlord's Objection at ¶ 2. The Landlord was not listed as a creditor in the Debtor's schedules.

The Debtor's chapter 13 plan was confirmed by Order, signed December 14, 2002 ("Confirmation Order"). It provides for direct payments on the lease to the "Peter Family Trust." According to the Landlord's counsel, a special proceeding was commenced in the Town of Clay Justice Court on or about July 15, 2003 as a result of the Debtor's alleged default in the payment of rent in January 2003. *See* Affidavit of Donald P. Colella, Esq., sworn to on October 29, 2003 ("Colella Affidavit") at ¶ 2. On or about July 16, 2003, Debtor's counsel, Stewart L. Weisman,

Esq. ("Weisman"), apprised Colella, who was representing the Landlord in the Town of Clay Justice Court, of the bankruptcy case. *See id.* By letter dated July 21, 2003, Colella requested withdrawal of the special proceeding from the Town of Clay Justice Court after being informed of the Debtor's case and his intention to convert to chapter 7. *See id.* at ¶ 3. According to Weisman, he also apprised Colella that the Debtor had vacated the premises in June 2003 and that the Debtor would not oppose a motion in the Bankruptcy Court that requested possession of the Premises. *See* Debtor's Motion at 2.

On August 4, 2003, the Landlord filed a motion ("Landlord's Motion") seeking an order (1) compelling the Debtor's surrender of the Premises pursuant to Code § 365(d)(4) and (2) relief from the automatic stay to allow the Landlord "to collect from the Debtor all rent due since entry of the Confirmation Order . . . from non-estate property." Landlord's Motion at ¶¶ 12-15. The "Wherefore" clause indicates that the Landlord is asking that the lease be deemed rejected as of September 2, 2003, and that the Debtor be compelled to surrender the Premises in broom clean condition and that the automatic stay be terminated to permit the Landlord

> to commence and continue a state court eviction proceeding with respect to the Lease to recover possession of the Premises and to permit Landlord to commence an action against the Debtor to recover, and collect from the Debtor, all past due rent due since entry of the Confirmation Order <u>solely from non-estate property</u> . . . ." (emphasis in original document).

Landlord's Motion at 5.

The Landlord's Motion was scheduled to be heard on August 19, 2003, but was adjourned to September 9, 2003, at the request of the Landlord, due to the conversion of the case on July 23, 2003, and the desire to have it heard on a chapter 7 hearing date. *See* Letter of August 11,

2003, from Landlord's counsel.[1] In the interim, on September 5, 2003, the chapter 7 trustee filed a Report of No Distribution based on a finding that the Debtor's estate had no non-exempt property to distribute.

No opposition to the Landlord's Motion was filed with the Court and, accordingly, the Court signed an Order granting the Landlord's Motion on September 22, 2003.[2] On October 1, 2003, the Debtor filed the Motion presently under consideration requesting that the fourth decretal paragraph be stricken pursuant to Fed.R.Bankr.P. 9024, incorporating Fed.R.Civ.P. 60(b). That paragraph provides:

> ORDERED, that the automatic stay is terminated so to permit the Landlord to commence and continue a state court eviction proceeding with respect to the Lease to recover possession of the Premises and to permit Landlord to commence an action against the Debtor to recover, and collect from the Debtor, all past due

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[1] The letter from the Landlord's bankruptcy counsel, Dawn Simmons, Esq. ("Simmons), dated and received by facsimile on August 11, 2003, refers to the motion having been filed by SBU Bank. Indeed, the Notice of the Landlord's Motion makes reference to SBU, but the Motion itself identifies 1105-1141 Broadway Corporation as the movant. The Affidavit of Service, filed with the Landlord's Motion, identifies BSB Bank & Trust Co. as the movant. While Weisman does not assert any confusion as to the origination of the Landlord's Motion, the Court must admit to a certain amount of confusion in reviewing the papers and the docket in the matter. This is particularly true given the fact that some of the docket entries indicate filings on behalf of SBU and others on behalf of "1105-1141 Broadway Corporation, Successor-in-Interest to SBU." This conflicts with the Landlord's assertions in both its Motion and its objection to the Debtor's Motion that The Peter Family Irrevocable Trust is the predecessor-in-interest to 1105-1141 Broadway Corporation.

[2] On September 12, 2003, Debtor's counsel faxed a letter to the Court requesting that the fourth decretal paragraph of the "proposed" order, as well as the first decretal paragraph, be stricken as overbroad. Debtor's counsel took the position that "there is no basis to allow the creditor to sue for or be awarded rent." In a second letter faxed on September 12, 2003, Debtor's counsel explained that it had been his understanding that the Landlord's Motion had been resolved without the need for him to appear on September 9, 2003. The Court responded on or about September 18, 2003, indicating its intent to execute the proposed order in its present form due to counsel's failure to interpose any opposition to the Landlord's Motion prior to the return date.

> rent due since entry of the Confirmation Order solely from non-estate property.

Weisman asserts that the Notice of Motion did not make any reference to a request for an administrative expense under Code § 348(d) or § 503(b), and "a motion for relief from the automatic stay should not qualify as a motion for administrative expense as is the case here." Debtor's Second Supplemental Memorandum, filed November 24, 2003.

At the hearing on December 2, 2003, Weisman admitted that he had perused only the first two pages of the Landlord's Motion. He indicated that he had not read it in its entirely because it was his understanding that the parties had reached an agreement simply for the Debtor to turn over the Premises to the Landlord. He was unaware that the Landlord was also seeking monetary damages. Simmons responded that the relief set forth in the Order was clearly requested in the Landlord's Motion, and that relief included being allowed to collect past due rents from non-estate property.

## DISCUSSION

A judgment by default may be set aside pursuant to Fed.R.Civ.P. 60(b), as incorporated in Fed.R.Bankr.P. 9024. Whether or not to reconsider a prior order obtained on default is within the sound discretion of the court. *See Enron Oil Corp. v. Diakuhara*, 10 F.3d 90, 95 (2d Cir. 1993) (citations omitted). The rule is not intended to abrogate the finality of judgments. Instead, Fed.R.Civ.P. 60(b) is to be applied in striking a balance between serving the ends of justice, including having the matter resolved on the merits, and preserving the finality of judgments. *See id.* at 95-96; *Nemaizer v. Baker*, 793 F.2d 58, 61 (2d Cir. 1986) (citation omitted). Fed.R.Civ.P.

60(b)(1) provides that a court may relieve a party from a final judgment or order based on mistake, inadvertence, or excusable neglect (emphasis added). In addition, Fed.R.Civ.P. 60(b)(6) provides for the same relief for "any other reason justifying relief from the operation of the judgment." However, relief from a prior judgment pursuant to Fed.R.Civ.P. 60(b)(6) is only to be granted if the party is able to show "extraordinary circumstances" that the party is faultless. *Pioneer Investment Services Co. v. Brunswick Associates Ltd. Partnership*, 507 U.S. 380, 393 (1993) (citations omitted). Otherwise, if the party is partly to blame, then relief must be based on a showing of "excusable neglect" pursuant to Fed.R.Civ.P. 60(b)(1). *Id.*

In considering a motion to set aside a default judgment or order on default based on Fed.R.Civ.P. 60(b)(1), as is the case herein, courts apply three factors: "(1) whether the default was willful; (2) whether setting aside the default would prejudice the adversary; and (3) whether a meritorious defense is presented." *Enron*, 10 F.3d at 96. These factors are to be considered in light of the fact that defaults "are generally disfavored and are reserved for rare occasions because there is a preference for resolving disputes on the merits." *Id.* at 95 (citations omitted). Furthermore, "when doubt exists as to whether a default should be granted or vacated, the doubt should be resolved in favor of the defaulting party. In other words, 'good cause' and the criteria of the Rule 60(b) set aside should be construed generously." *Id.* at 96 (citations omitted).

A. Willfulness of Default

> Willfulness does not include mere carelessness or negligence but does encompass gross negligence, deliberateness, and bad faith; the degree of willfulness determines how heavily the factor

> weighs against granting relief. (citations omitted) . . . But if a defendant's default was willful and the defendant had no meritorious defense, an absence of prejudice to the plaintiff will not entitle the defendant to relief from a default judgment.

*RLS Associates, LLC v. United Bank of Kuwait PLC*, 2002 WL 122927 at *3 (S.D.N.Y. Jan. 29, 2002) (citations omitted).

In this case, Weisman does not deny receiving the Landlord's Notice and Motion. The caption of the Notice indicates that the Landlord is requesting that the Debtor surrender the leased premises pursuant to Code § 365(d)(4) and that the automatic stay be terminated pursuant to Code § 362(d)(1). There is nothing in the Notice to indicate that the Landlord is seeking an administrative expense pursuant to Code § 503(b) or that it intends to collect past due rent from the date of entry of the Confirmation Order. Weisman acknowledges having only read the first two pages of the Landlord's Motion. It is on page 4 of the Landlord's Motion that relief from the automatic stay is requested to permit the Landlord to collect the past due rents. *See* Landlord's Motion at 4. The Landlord goes on to request, in the alternative, that the automatic stay be terminated in order for the Landlord to commence an eviction proceeding and to recover possession of the Premises. *Id.* at 4. In the body of the latter request is mention of the fact that the Landlord also was requesting that it be permitted to collect all past due rent from non-estate property of the Debtor. *Id.* at 5. The "Wherefore" clause, as noted previously, seeks all such relief. *Id.*

Weisman indicates that he did not read the Landlord's Motion in its entirety based on his prior conversation with Colella and his understanding that they had reached an agreement whereby the Debtor would surrender the Premises. He stated that he had suggested that Colella seek relief from the automatic stay as a mere formality since the Debtor had already vacated the

Premises in June 2003. According to Weisman, he had indicated that he would not oppose any such motion due to the anticipated conversion of the Debtor's case to chapter 7.

Weisman's reliance on his understanding of the relief being sought based on his conversation with Colella, as well as his reliance on the caption of the Landlord's Notice and Motion, was a dangerous practice and demonstrates some degree of negligence on his part. However, it certainly does not rise to the level of bad faith or gross negligence. Furthermore, the Court is mindful of the Second Circuit's view that default judgments are "reserved for rare occasions." *Enron*, 10 F.3d at 95. Accordingly, the Court will give little weight to this factor if it determines that the Debtor has a meritorious defense to allowing the Landlord to collect past due rents that accrued after the Debtor's plan was confirmed in the chapter 13.

B. Merits of Debtor's Defense

While the Landlord's counsel argues that it is seeking an administrative claim under Code § 503(b) based on occupancy of the Premises, Debtor's counsel contends that the Notice and Motion made no mention of seeking an administrative claim for the post-confirmation rent. It is the Debtor's position that the Landlord is not entitled to such rent and that the Debtor was entitled to discharge any such debt upon conversion to chapter 7.

Code § 1307(a) allows a debtor to convert a case from chapter 13 to a case under chapter 7. Code § 348(b), which addresses the effect of conversion, provides that the date of "the order for relief" in a converted case refers to the date of conversion for purposes of various sections of the Code, including § 727(b). *See In re Toms*, 229 B.R. 646, 653 (Bankr. E.D. Pa. 1999) (citations omitted). However, Code § 348(d) specifies that claims against the estate or the debtor that arise before conversion "shall be treated for all purposes as if such claim had arisen

immediately before the date of the filing of the petition," with the exception of claims specified in Code § 503(b), namely administrative expenses.

> Section 348(d) deals with the treatment of claims. It should be construed to provide that non-administrative claims arising in a chapter 11, upon conversion, are treated as prepetition debts. Chapter 11 administrative claims are provided for differently. They retain their priority status and are paid ahead of unsecured creditors in the case. They are inferior, however, to chapter 7 administrative expenses. 11 U.S.C. § 726(a)(1) and § 726(b).
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> Section 727(b), on the other hand, deals with the discharge of these chapter 11 claims. Read in conjunction with § 348(a) and (b), it provides that unless a debt is excepted from discharge under § 523, a discharge under § 727(a) discharges the debtor from all debts "that arose before the date of the order for relief under this chapter." . . . Thus, § 727(b) specifically discharges the debtor from all debts arising before the date of conversion. The only exceptions are those provided under 11 U.S.C. § 523.

*In re Ramaker*, 117 B.R. 959, 962-963 (Bankr. N.D. Iowa 1990); *see also In re Pavlovich*, 952 F.2d 114, 118 (5th Cir. 1992) (noting that "Section 348(d) simply does not address the availability of remedies against discharge and dischargeability. If it did, it would conflict with §§ 348(a) and (b), which, taken together, specifically incorporate §§ 727 and 523 in the converted case. . . . Section 348(d) governs the relative priorities of pre-petition and post-petition-pre-conversion claims." (citation omitted)).

The court in *Toms* recognized the applicability of the *Ramaker* conclusions to a chapter 13 case and determined that a debtor is discharged of all debts which arose before the date of conversion unless they are determined to be nondischargeable pursuant to Code § 523(a). *See Toms*, 229 B.R. at 653-54. To bolster its conclusion that debts based on administrative expense claims were dischargeable pursuant to Code § 727(b), unless excepted pursuant to Code § 523,

the court in *Toms* also examined the legislative history of Code § 727(b):

> "Section 727(b) of the House amendment adopts a similar provision contained in the Senate amendment modifying the effect of discharge. The provision makes clear that the debtor is discharged from all debts that arose before the date of the order for relief under chapter 7 . . . *Thus, if a case is converted from chapter 11 or chapter 13 to a case under chapter 7, all debts prior to the time of conversion are discharged* . . . . This modification is particularly important with respect to an individual debtor who files a petition under chapter 11 or 13 of title 11 if the case is converted from another chapter to chapter 7, or whether the other chapter proceeding is dismissed and [a] new case is commenced by filing a petition under chapter 7."

*Toms*, 229 B.R. at 655, quoting 124 Cong. Rec. H11098 (daily ed. Sept. 28, 1978) (statement of Rep. Edwards); 124 Cong. Rec. S17415 (daily ed. Oct. 6, 1978) (statement of Sen. DeConcini) (emphasis added).

Finally, the court in *Toms* examined Fed.R.Bankr.P. 1019(5) and (6), as well as Fed.R.Bankr.P. 3002, in finding that those rules also "recognize that pre-conversion administrative claims, albeit priority claims, will be treated as dischargeable claims in the converted chapter 7 case." *Toms*, 229 B.R. at 655. Specifically, Fed.R.Bankr.P. 1019(6), applicable to postpetition, preconversion administrative expenses, states that "[a] claim of a kind specified in § 348(d) may be filed in accordance with Rules 3001(a)-(d) and 3002." Payment on such claims, however, are predicated on there being sufficient assets in the estate. In this case, the chapter 7 trustee filed a report on September 5, 2003, indicating that there were no non-exempt assets available for distribution to creditors.

The court in *Toms* concluded that "[t]aken together, the express language of the relevant statutory provisions, the persuasive legislative history, and the procedural requirement imposed upon all pre-conversion claimants make clear that Congress intended to render such claims

dischargeable, even those granted priority as chapter 13 administrative claims." *Toms*, 229 B.R. at 656.

The Court declines to follow the holding in *Babb*s, 265 B.R. 35, *supra*, that post-petition, pre-conversion rental arrears are exempt from discharge. The court in *Babbs* based its conclusion on "Code § 365(d)(1)(A)," a statutory provision which does not exist, and this Court has been unable to discover any other statutory basis for such a finding. Instead, this Court finds the analysis of *Toms*, as well as the discussion in *Ramaker,* persuasive and concludes that the Landlord's claim, even if it warranted priority status as an administrative claim, was discharged, unless otherwise excepted under one of the provisions of Code § 523 to which Fed.R.Bankr.P. 4007(d)[3] is inapplicable. *See also In re Fickling*, 277 B.R. 168, 170 (Bankr. E.D.N.Y. 2002) (incorporating the reasoning of *Toms* and *Ramaker* in determining that counsel fees which were incurred pre-conversion in a chapter 11, although entitled to an administrative expense claim, were dischargeable in the chapter 7 in the event that estate assets were insufficient to satisfy them). According to the notice sent out to all creditors after the conversion of the Debtor's case, the last day to oppose the discharge of the debtor or to determine the dischargeability of certain debts was November 4, 2003. According to the docket in the case, the Order discharging the Debtor was entered on November 6, 2003. There is nothing in the docket to indicate that the Landlord filed a complaint seeking to have the Debtor denied a discharge or seeking a determination that the debt owed to it was nondischargeable. The Court concludes that the Debtor's assertion that the Landlord is not entitled to collect the rents due on the Premises after

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[3] Fed.R.Bankr.P. 4007(c) requires that "[a] complaint to determine the dischargeability of a debt under § 523(c) shall be filed no later than 60 days after the first date set for the meeting of creditors under § 341(a)."

confirmation of the Debtor's plan in the chapter 13 and prior to conversion to chapter 7, regardless of the property from which the rent collection would occur, is a meritorious defense in support of its motion.

C. Prejudice to the Landlord

The hearing on the Landlord's Motion was held on Tuesday, September 9, 2003. On Friday, September 12, 2003, Weisman faxed a letter to the Court objecting to the language in the proposed order he had received following the hearing. The Order was signed on September 22, 2003, in spite of his objection, due to his failure to file opposition to the Landlord's Motion or to appear at the hearing. This Motion was filed approximately nine days later on October 1, 2003. Thus, there has been little delay that would somehow prejudice the rights of the Landlord. There are also no allegations of fraud or collusion that might, otherwise, support a finding of prejudice. *See In re Emmerling*, 223 B.R. 860, 869 (2d Cir. BAP 1997). Accordingly, the Court concludes that the Debtor has established a basis for vacating the Order of September 22, 2003, which was previously granted on default.

Based on the foregoing, it is hereby

ORDERED that the fourth paragraph of the Order signed, September 22, 2003, is hereby vacated and stricken to the extent that it permitted the Landlord to commence an action against the Debtor to recover and collect from the Debtor, all past due rent due since entry of the Confirmation Order solely from non-estate property; it is further

ORDERED that the Debtor's counsel file with the Court, and serve on the Landlord's counsel, an Amended Order consistent with the terms herein.

Dated at Utica, New York

this 21st day of January 2004

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STEPHEN D. GERLING
Chief U.S. Bankruptcy Judge