

**UNITED STATES BANKRUPTCY COURT  
WESTERN DISTRICT OF NEW YORK**

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**In re:**

**CASE NO. 98-23000**

**JOHN PETER HART and MARJORIE ELAINE HART,**

**Debtors.**

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**RURAL OPPORTUNITIES, INC.,  
COUNTY OF ONTARIO AND GENESEE  
FINGER LAKES REGIONAL PLANNING  
(GENESEE FINGER LAKES REGIONAL  
PLANNING COUNCIL),**

**DECISION & ORDER**

**Plaintiffs,**

**AP #98-2216**

**V.**

**JOHN PETER HART and MARJORIE ELAINE HART,**

**Defendants.**

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**BACKGROUND**

On August 10, 1998, the “Debtors,” “John Hart” and “Marjorie Hart,” filed a petition initiating a Chapter 7 case. On the schedules and statements required to be filed by Section 521 and Rule 1007, the Debtors indicated that: (1) John Hart was a 51% shareholder of RCSA, Inc. and had guaranteed loans made to RCSA, Inc. by: (a) The City of Geneva IDA (“Geneva”); (b) Rural Opportunities, Inc. (“Rural Opportunities”); (c) Ontario County (“Ontario”); and (d) Genesee Finger Lakes Regional Planning Council (“Finger Lakes”); and (2) they owned a 19' boat.

On August 20, 1998, a Notice was sent by the Bankruptcy Court to all creditors which indicated that a Section 341 Meeting of Creditors (the "341 Meeting") would be held on September 16, 1998, and that November 16, 1998 was the deadline to file complaints to object to the Debtors' discharge or to request a determination of the dischargeability of any debts (the "Bar Date"). On September 4, 1998, a Notice was sent to all creditors by the attorney who represented the Debtors when they filed their petition. The Notice indicated that, due to that attorney's unavailability, the 341 Meeting was being adjourned to October 6, 1998. On October 6, 1998, an initial 341 Meeting was conducted by the Debtors' "Trustee," at which time the Debtors were represented by a new attorney, and the Meeting was adjourned to October 21, 1998. The Trustee's Minute Report of the initial 341 Meeting indicated that representatives of Rural Opportunities and Ontario attended the Meeting.

On October 16, 1998, the Debtors filed a number of amended schedules and statements, along with an amendment cover sheet dated October 5, 1998 signed by the Debtors' new attorney (the "Amended Schedules"). The Amended Schedules set forth: (1) John Hart's ownership of stock in RCSA, Inc., and various names that it operated under, as well as a personal d/b/a, Adteck Marketing; (2) the Debtors' ownership of a boat trailer; and (3) various judgments that had been taken against John Hart, including judgments by Rural Opportunities and Ontario.

The Trustee's Minute Report of the adjourned 341 Meeting conducted on October 21, 1998 indicated that: (1) possible nonexempt assets in the estate included the now-scheduled boat trailer; and (2) representatives of Rural Opportunities, Ontario and Geneva attended the adjourned Meeting.

On November 6, 1998, the Debtors filed a motion pursuant to Section 522(f) (the “Avoidance Motion”), which requested an order avoiding the judgment liens of Rural Opportunities and Ontario on their residence. On November 13, 1998, Rural Opportunities and Ontario interposed Opposition to the Avoidance Motion which alleged that: (1) the fair market value of the Debtors’ residence was significantly greater than the value alleged in the Motion; and (2) Rural Opportunities and Ontario intended to file adversary proceedings pursuant to Sections 727 and 523 objecting to the Debtors’ discharge, and to the discharge of their individual judgment debts, so that a determination on the avoidability of the judgment liens should await final determinations in the adversary proceedings. On November 19, 1998, the Debtors interposed a Reply to the Opposition of Rural Opportunities and Ontario which alleged that: (1) Section 522(c) made it irrelevant to the 522(f) relief requested by the Debtors whether or not Rural Opportunities or Ontario succeeded in any adversary proceeding commenced pursuant to Sections 727 or 523; and (2) an appraisal obtained post-petition by the Trustee indicated that there was in fact no nonexempt equity in the Debtors’ residence. At a final hearing on the Avoidance Motion conducted by the Court on January 6, 1999, Rural Opportunities and Ontario indicated that, because of the fair market value of the Debtors’ residence, as indicated by the Trustee’s appraisal, they were withdrawing their Opposition.

On October 16, 1998, Geneva filed a motion (the “Extension Motion”) which requested that the Court extend its time to object to the Debtors’ discharge, pursuant to Section 727, or to the dischargeability of its debt from John Hart, pursuant to Section 523. The Motion, among its other allegations, stated that, because Geneva had been unable to fully examine the Debtors, it was “unable to determine if cause exists to raise an objection to discharge under 11 U.S.C. §727 and/or 11 U.S.C.

§523.” On November 20, 1998, and December 22, 1998, the Debtors interposed Opposition to the Extension Motion. The Opposition asserted that Geneva had completely failed to demonstrate that: (1) there was any “cause” for an extension, as required by Rules 4004(b) and 4007(c); and (2) prior to the Bar Date, it had exercised due diligence to determine whether: (a) it had a cause of action under either Section 727 or Section 523; and (b) there was any cause sufficient to allow the Court, in its discretion, to extend Geneva’s time for the filing of a complaint. At a final hearing on the Extension Motion conducted by the Court on January 6, 1999, Geneva withdrew its Motion.

On November 16, 1998, Rural Opportunities, Ontario and Finger Lakes (the “Plaintiffs”) filed a single adversary proceeding (the “Adversary Proceeding”) against both John Hart and Marjorie Hart which requested that the Court: (1) determine the indebtedness due to each of the Plaintiffs to be nondischargeable, pursuant to Section 523(a)(2)(A), because the Debtors, through false pretenses, false representations and/or actual fraud had acted to induce the Plaintiffs to enter into certain loan agreements; (2) determine the indebtedness due to each of the Plaintiffs to be nondischargeable, pursuant to Section 523(a)(4), because, upon information and belief, the Debtors had engaged in fraud or defalcation while acting in a fiduciary capacity, embezzlement or larceny; and (3) deny the Debtors a discharge, pursuant Section 727, because: (a) the Debtors, with the intent to hinder, delay and defraud the Plaintiffs, upon information and belief, had transferred, removed, destroyed, mutilated, or concealed, or had permitted to be transferred or removed, destroyed, mutilated or concealed, property of the Debtors within one year prior to the filing of their bankruptcy; (b) the Debtors had concealed, destroyed, mutilated, falsified or failed to keep or preserve any recorded information from which their financial condition or business transactions

might be ascertained; (c) the Debtors had knowingly and fraudulently made false accounts at the 341 Meeting; and (d) the Debtors were unable to satisfactorily explain a loss of assets utilized in the operation of a business.

On November 19, 1998, the Debtors filed a motion (the “Dismissal Motion”) which requested an Order dismissing the Adversary Proceeding on the grounds that the Plaintiffs’ Complaint failed to state any claims upon which relief could be granted. The Dismissal Motion alleged that: (1) the Complaint was utterly devoid of factual content; (2) with regard to the cause of action pursuant to Section 523(a)(2)(A), the Complaint failed to particularize the allegations of false pretenses, false representations and/or actual fraud, the falsity of the representations and the Debtors’ knowledge of the falsity, as required by The Federal Rules of Bankruptcy Procedure and The Federal Rules of Civil Procedure; (3) with regard to the cause of action pursuant to Section 523(a)(4), the Complaint failed to set forth any facts or allegations particularizing any alleged fraud or defalcation, failed to set forth the particulars of any alleged fiduciary relationship that the Debtors had, and did not set forth in detail what was allegedly stolen or embezzled; (4) with regard to the cause of action pursuant to Section 727(a), the Complaint failed to set forth any facts particularizing any acts, conduct or omissions that could result in the denial of a discharge.

On December 4, 1998, the Plaintiffs interposed an Answering Affidavit by their attorney (the “Answering Affidavit”) which alleged that: (1) the Plaintiffs had the right to move to amend the Complaint, and, under the Federal Rules, leave was generally freely given if justice so required it; (2) the Debtors could request interrogatories to gain information with regard to the particularities of

the causes of action set forth in the Complaint; (3) the attorney who filed the Complaint had been retained only one day prior to the last day to file complaints; (4) the Plaintiffs had advised their attorney that the Debtors had made a false oath at the 341 Meeting and that in making loans to John Hart, the Plaintiffs had relied on a June 4, 1993 financial statement of the Debtors, a copy of which was attached to the Affidavit; (5) a list of equipment located at RSCA, Inc. on or about October 19, 1998<sup>1</sup> that was attached to the Affidavit, was different from another attached equipment list, apparently provided to the Plaintiffs in 1993 when their loans were made to RSCA, Inc. and guaranteed by John Hart; (6) John Hart had a bank account with the Bank of Ireland that had not been disclosed in his schedules and statements; and (7) the Plaintiffs needed thirty days to review the 341 Meeting tapes and amend their Complaint to particularize their claims against the Debtors.

On December 8, 1998, the Debtors filed an Affidavit by John Hart (the "Hart Affidavit") in support of the Dismissal Motion. The Hart Affidavit alleged that: (1) the Debtors' June 4, 1993 Financial Statement, a copy of which was attached to the Answering Affidavit, was in all respects correct when issued; (2) the 1993 Equipment List attached to the Answering Affidavit was provided to the Plaintiffs' agent, Niagara Small Business Lending Center, which fully understood the contents of the list at the time; (3) the Debtors never had an account at the Bank of Ireland; (4) the Plaintiffs knew about John Hart's Adteck Marketing d/b/a, since they had previously received payments from Adteck Marketing; (5) Marjorie Hart was not indebted to the Plaintiffs, so there was no debt which could be determined by the Court to be nondischargeable pursuant to Section 523; and (6) nothing

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<sup>1</sup> It appears that this date should have been October 19, 1997.

in the Answering Affidavit explained or justified why the Complaint in the Adversary Proceeding did not set forth any specific facts to support the Plaintiffs' alleged causes of action.

At the December 9, 1998 initial return date of the Dismissal Motion, the Court dismissed the Plaintiff's cause of action pursuant to Section 523(a)(4).<sup>2</sup> The Court determined that: (1) the Complaint, which merely tracked the language of Section 523(a)(4), failed to set forth any facts whatsoever to establish that the debts due to the Plaintiffs were the result of fraud or defalcation on the part of either of the Debtors while acting in a fiduciary capacity, or that the Debtors had committed embezzlement or larceny; (2) even if the Court considered the allegations set forth in the Answering Affidavit and any arguments made by the attorney for the Plaintiffs at the initial return date of the Dismissal Motion, which would require it, pursuant to the provisions of Rule 12(c) of the Federal Rules of Civil Procedure,<sup>3</sup> as incorporated into Rule 7012, to treat the motion as one for

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<sup>2</sup> Section 523(a)(4) provides that:

(a) A discharge under section 727, 1141, 1228(a), 1228(b), or 1328(b) of this title does not discharge an individual debtor from any debt-

(4) for fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny;

11 U.S.C. §523(a)(4) (1999).

<sup>3</sup> Rule 12(c) of the Federal Rules of Civil Procedure provide that:

(c) Motion for Judgment on the Pleadings. After the pleadings are closed but within such time as not to delay the trial, any party may move for judgment on the pleadings. If, on a motion for judgment on the pleadings, matters outside the pleadings are presented to and not excluded by the court, the motion shall be treated as one for summary judgment and disposed of as provided in Rule 56, and all parties shall be given reasonable opportunity to present all material made pertinent to such a motion by Rule 56.

FRCP Rule 12(c) (1999).

summary judgment, the Plaintiffs had failed to establish any disputed material fact, or that the Debtors had acted in a fiduciary capacity with respect to the Plaintiffs, or that they had committed embezzlement or larceny; and (3) none of the Plaintiffs even had a debt due from Marjorie Hart that the Court could determine to be nondischargeable pursuant to Section 523(a)(4). At the conclusion of the December 9, 1998 initial hearing on the Dismissal Motion, the Court adjourned the Motion to January 6, 1999, and afforded the Plaintiffs a further opportunity to file affidavits containing sufficient factual allegations to demonstrate that they had a cause of action against the Debtors under Section 523(a)(2)(A) or Section 727(a).

On January 5, 1999, the attorney for the Plaintiffs submitted an additional affidavit (the "Attorney Affidavit") which alleged that: (1) the attorney had spoken with George Buksar ("Buksar"), a former co-owner of RCSA, Inc. with John Hart; (2) Buksar had left RCSA, Inc. in December of 1996; (3) Buksar believed that in December 1996, RCSA, Inc. had sufficient raw materials to construct fifteen bus shelters; (4) on or about October 15, 1997, RCSA, Inc. was evicted from its business premises in Geneva; (5) the October 1997 Equipment List attached to the Answering Affidavit did not contain enough equipment to build fifteen bus shelters; (6) in May 1997, John Hart had filed a certificate to do business under the name of Adteck Marketing; (7) in August 1998, Buksar observed a business premises in Rochester, New York where bus shelters were being completed utilizing what he believed was the same inventory that had been located at the Geneva location of RCSA, Inc.; (8) Buksar advised the attorney for the Plaintiffs that the Rochester business premises were being operated by Adteck Marketing; (9) at the 341 Meeting of Creditors, Hart had denied that he removed any equipment or assets from the Geneva location of RCSA, Inc. that were collateral for the obligations owed to the Plaintiffs, and further denied that he used any such assets for a business conducted by Adteck Marketing in Rochester; (10) the Debtors had failed



to list the Adteck Marketing business in their schedules; and (11) Plaintiffs should be allowed to amend their Complaint with this information to support their cause of action pursuant to Section 727(a).

On January 6, 1999, the Plaintiffs filed an affidavit by Buksar (the "Buksar Affidavit") which essentially confirmed the relevant allegations that had been set forth in the Attorney Affidavit, and further alleged that Buksar had been advised by a third-party that prior to RCSA, Inc. being evicted in October 1997, a moving van appeared at the Geneva premises and removed raw material and inventory from the premises.

At the January 6, 1999 adjourned hearing on the Dismissal Motion, the Court dismissed the Plaintiffs' cause of action pursuant to Section 523(a)(2)(A).<sup>4</sup> The Court determined that: (1) the Complaint, which merely tracked the language of Section 523(a)(2)(A), failed to set forth any facts whatsoever to establish that the debts due to the Plaintiffs were for money, property, services or an extension, renewal or refinance of credit that was obtained by the Debtors by false pretenses, false representation or actual fraud; (2) even if the Court considered the allegations set forth in the Answering Affidavit, Attorney Affidavit and Buksar Affidavit, and any arguments made by the attorney for the Plaintiffs, and treated the Motion as one for summary judgment, the Plaintiffs had

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<sup>4</sup> Section 523(a)(2)(A) provides that:

(a) A discharge under section 727, 1141, 1228(a), 1228(b), or 1328(b) of this title does not discharge an individual debtor from any debt—

(2) for money, property, services, or an extension, renewal, or refinancing of credit, to the extent obtained by—

(A) false pretenses, a false representation, or actual fraud, other than a statement respecting the debtor's or an insider's financial condition;

failed to establish any disputed material fact, or that either Debtor had obtained any property or credit by false pretenses, false representations or actual fraud; (3) the Attorney Affidavit, which requested that the Plaintiffs be able to amend their Complaint in connection with their Section 727(a) cause of action, indirectly conceded that with the information developed in connection with the Dismissal Motion, the Plaintiffs had no valid Section 523(a)(2)(A) cause of action; and (4) none of the Plaintiffs even had a debt due from Marjorie Hart that the Court could determine to be nondischargeable pursuant to Section 523(a)(2)(A). At the conclusion of the January 6, 1999 adjourned hearing on the Dismissal Motion, the Court adjourned the Motion for a final hearing regarding the Plaintiff's Section 727(a) causes of action.

On January 19, 1999, John Hart filed an additional affidavit (the "Hart 727 Affidavit") which alleged that: (1) RCSA, Inc. had been in the business of manufacturing, selling and leasing computerized rotational outdoor advertising signs and other advertising structures; (2) one of its customers had been PEM Action View ("PEM") of Vancouver, British Columbia; (3) in 1996, because RCSA, Inc. was unable to finance the acquisition of the raw materials necessary to complete the finished goods which PEM had ordered, PEM, in cooperation with the U.S. Small Business Administration and the First National Bank of Rochester, supplied letters of credit to finance the purchase by RCSA, Inc. of the raw materials that it required for the construction of the bus shelters ordered by PEM; (4) in October 1997, when the landlord of the RCSA, Inc. business premises in Geneva threatened to evict the corporation, PEM took possession of the raw materials and the partially finished bus shelters being constructed for PEM, and shipped them to their business premises in Vancouver, British Columbia; (5) the individual representing PEM in connection with the removal of the raw materials and inventory was Mr. Rick Mari ("Mari"); (6) after the RCSA, Inc. business was terminated by eviction in October 1997 and PEM's raw materials and inventory had

been removed to Vancouver, PEM inquired as to whether Hart, who was then unemployed, would work with them to complete some of the unfinished bus shelters; (7) Hart agreed to work for PEM; (8) in December 1997, the raw materials and inventory removed by PEM to Vancouver were shipped to Rochester to a location which Hart had helped Mari locate; (9) PEM entered into a month-to-month lease of the "Rochester Facility"; and (10) in January 1998, Hart obtained full-time employment and ceased any efforts on behalf of PEM.

On January 19, 1999, the attorney for the Plaintiffs filed an additional affidavit which indicated that he had contacted the landlord of the Rochester Facility who had confirmed that a month-to-month lease had been negotiated by Hart and an individual from PEM, but that it had been signed only by PEM.

On January 29, 1999, the Debtors filed an affidavit by Mari (the "Mari Affidavit") which alleged that: (1) because of the letter of credit which PEM had supplied in connection with the First National Bank of Rochester financing of the purchase by RCSA, Inc. of raw materials to complete the PEM orders, he, as its employee, and PEM had viewed those raw materials and any partially manufactured but undelivered bus shelters to be the property of PEM; (2) in October 1997, when he believed that the RCSA, Inc. operations would be terminated by eviction, he took possession of the PEM raw materials and partially completed bus shelters, on behalf of PEM, and he had them shipped to Vancouver by common carrier; (3) he later asked John Hart and some of the former RCSA, Inc. employees to help PEM to complete unfinished shelters and build additional bus shelters, and he requested that Hart find a suitable location for a production facility; (4) on behalf of PEM, he had entered into a month-to-month lease of the Rochester Facility with the landlord, Mr. Resnick, and he had arranged for the raw materials and inventory which had been returned to Vancouver to be shipped to the Rochester Facility; (5) thereafter, PEM purchased additional raw materials for the

operations; (6) because of its own financial problems, PEM stopped operations at the Rochester Facility; (7) Mari believed that thereafter, sometime in the Summer of 1998, the landlord disposed of the remaining inventory to satisfy his back rent claims; (8) John Hart did not remove the PEM raw materials and partially completed shelters from the Geneva operations of RCSA, Inc., Mari did; and (9) John Hart had no ownership interest in any of the raw materials and shelters removed by PEM from Geneva, or in new inventory and raw materials purchased by PEM for the Rochester operation.

At the February 3, 1999 adjourned hearing on the Dismissal Motion, the Court: (1) dismissed the Plaintiff's entire Complaint as to the Debtor, Marjorie Hart, since none of the factual allegations made by the Plaintiffs in connection with the Dismissal Motion indicated that there was any cause of action against her pursuant to Section 727(a); and (2) allowed the parties to make any additional submissions they wished regarding the Plaintiff's Section 727(a) causes of action against the Debtor, John Hart.

A February 10, 1999 letter submission by the attorney for the Debtors pointed out that Buksar had previously filed a bankruptcy proceeding in this Court.<sup>5</sup>

A February 15, 1999 letter submission by the attorney for the Plaintiffs stated that, "The Supplemental Affidavits that have been submitted to this Court suggest that there is clearly a question of fact as to ownership of the raw materials used to construct bus stations and whether or not the same were converted by Mr. Hart for his own personal use or gain."

### DISCUSSION

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<sup>5</sup> A review of the Court's records indicated that: (1) on December 30, 1997, Buksar filed a petition initiating a Chapter 7 case; (2) on his schedules and statements, Buksar indicated that he was indebted to each of the Plaintiffs, as well as Geneva and First National Bank in connection with his guarantees of the obligations of RCSA, Inc.; (3) on April 10, 1998, Buksar received a discharge; and (4) on July 14, 1998, a final decree was entered and Buksar's no asset Chapter 7 case was closed.

## I. Overview

One of the fundamental policies of the Bankruptcy Code is to afford “honest” debtors a fresh start by discharging their pre-petition debts. However, Congress has limited this fresh start and discharge in the case of certain debts, enumerated in Section 523(a), which it has determined should not be discharged. In addition, Congress has determined that less than “honest” debtors, or debtors who have not performed the duties the Bankruptcy System requires of them, should not only have their discharge denied or revoked, if the requirements of Section 727 have been met, but they should also have their non-exempt assets marshaled, liquidated and distributed to creditors.

The tension created by Congress between, on the one hand, affording an “honest” debtor a discharge and a fresh start as soon as possible, and, on the other hand, insuring that: (1) even an otherwise honest debtor does not receive a discharge from a nondischargeable debt enumerated in Section 523(a); and (2) a dishonest or uncooperative debtor does not receive a discharge, is heightened by the relatively short period of time which Congress has afforded to interested parties to commence an Adversary Proceeding in the Bankruptcy Court to obtain a determination of causes of action under Section 727(a) and certain causes of action under Section 523(a). This period, set by Rule 4004(a) for certain causes of action under Section 523(a), and Rule 4007(c) for causes of action under Section 727(a), is sixty (60) days following the first date set for the Meeting of Creditors required by Section 341. In a Chapter 7 or 11 case, Rule 2003 requires that this Meeting be held in most cases no less than twenty days and no more than forty days after a voluntary petition is filed. As a result, the Bar Date in most cases will be a date from between eighty (80) and one hundred (100) days after the filing of the petition.

When a creditor has been engaged in pre-petition collection activities and obtained knowledge about a debtor’s financial affairs, especially as they relate to the creditor’s debt, the time

between the filing of the petition and the Bar Date may be sufficient for that creditor to file a complaint which sets forth specific and detailed facts that demonstrate a cause of action under Sections 523(a) or 727(a). However, when a creditor has not been engaged in any significant pre-petition collection activities, or where the debtor's trustee believes that a Section 727(a) cause of action may exist, this time between the petition and the Bar Date can seem very short.

Nevertheless, this is the period of time that Congress has established. Therefore, creditors and trustees must begin taking steps as soon as possible in the bankruptcy proceeding to investigate the debtors' affairs, gather any necessary information and documentation, and exercise due diligence to determine whether any causes of action exist under Sections 523(a) or 727(a). In some circumstances, even with due diligence, creditors and trustees will require more time, and the Rules provide that if they can establish cause before the Bar Date, the court can extend the Bar Date.

## **II. Extensions For Cause**

In connection with complaints requesting a determination of the dischargeability of those debts enumerated in Section 523(a) that are subject to the Bar Date, Rule 4007(c) provides that: "on motion of any party in interest after hearing on notice the court may for cause extend the time fixed under this subdivision. The motion shall be made before the time has expired."

In connection with complaints requesting the denial of a discharge under Section 727(a), Rule 4004(b) provides that: "on motion of any party in interest, after hearing on notice, the court may extend for cause the time for filing a complaint objecting to discharge. The motion shall be made before such time has expired."

In determining whether to exercise its discretion to grant an extension of the Bar Date for cause, courts, including this Court, have uniformly required that creditors and trustees demonstrate that they have exercised due diligence prior to the Bar Date in gathering necessary facts and

supporting documents to determine whether a good faith cause of action exists to object to a discharge or the dischargeability of a debt. See *In re Desiderio*, 209 B.R. 342 (Bankr. E.D.Pa. 1997); *In re Mendelsohn*, 203 B.R. 831 (Bankr. S.D.N.Y. 1996); and *In re Farhid*, 171 B.R. 94 (Bankr. N.D.Ca. 1994).

In determining whether cause exists to grant an extension of the Bar Date for both objections to discharge and the dischargeability of a debt, courts should employ a totality of the circumstances approach and consider all relevant facts and circumstances, including, but not limited to: (1) the due diligence exercised by the creditor or the trustee requesting the extension; (2) the complexity of the debtor's affairs; (3) the debtor's cooperation before the Bar Date in meeting reasonable requests by the creditor or the trustee for relevant information or documentation; (4) whether the debtor would be prejudiced by any reasonable extension of the Bar Date; and (5) whether there appears to be a reasonable factual and legal basis for the creditor or the trustee to believe that a cause of action exists under Sections 523(a) or 727(a).

It is this Court's experience, and continuing expectation, that if a creditor or a trustee has exercised due diligence in connection with a potential cause of action under Section 523(a) or Section 727(a), and the debtor, after reviewing the totality of the circumstances, realizes that under Rule 4004(b) or 4007(c) the creditor or trustee can establish the necessary cause to obtain a reasonable extension of the Bar Date, at the request of that creditor or trustee, the debtor should enter into a stipulation for a reasonable extension of the Bar Date. As a result, the Court should hear motions for a reasonable extension of the Bar Date only when there is a genuine dispute as to whether cause exists.

In this case, had the Plaintiffs filed a motion for an extension of the Bar Date to file a complaint under Sections 523(a)(2)(A) or 523(a)(4), based upon the factual allegations contained

in the Answering Affidavit, this Court would have denied the motion, because the Plaintiffs would not have established the required cause. The Court, in reviewing the totality of the circumstances, would have concluded that the Plaintiffs had not demonstrated sufficient due diligence or a sufficient factual and legal basis to support a Section 523(a)(2)(A) or 523(a)(4) cause of action against either of the Debtors, or even a sufficient basis to obtain an extension of the Bar Date for cause. The Court would have considered the following as significant factors in determining the exercise of due diligence and the existence of cause: (1) Rural Opportunities had taken a judgment against John Hart on July 9, 1997, over one year prior to the filing of his petition and before the RCSA, Inc. business operations had terminated in Geneva; (2) Ontario had taken a judgment against John Hart on January 30, 1998, more than seven months before the filing of his petition and after the RSCA, Inc. business operations had terminated in Geneva; (3) RSCA, Inc. had ceased operations and been evicted from its business premises in Geneva in October 1997, more than nine months before the filing of the Debtors' petition; (4) Buksar, a co-owner of RSCA, Inc. and a co-guarantor on all of the Plaintiffs' obligations, had filed a Chapter 7 case in December 1997, more than seven months before the filing of the Debtors' petition and after the RCSA, Inc. business operations had terminated in Geneva, and Buksar had listed the Plaintiffs as creditors; and (5) representatives of Rural Opportunities and Ontario had been present at both of the 341 Meetings conducted on October 6 and on October 21, 1998.

**III. Motions to Dismiss Complaints Under Section 523(a) or Section 727(a) For a Failure to State a Cause of Action**

**A. General**

Rule 8(a)(2) of the Federal Rules of Civil Procedure, made applicable by Rule 7008, requires that a pleading which sets forth a claim for relief contain a short and plain statement of the claim showing that the pleader is entitled to relief.



Rule 8(f) of the Federal Rules of Civil Procedure, requires that all pleadings be construed to do substantial justice.

Rule 9(b) of the Federal Rules of Civil Procedure, made applicable by Rule 7009, requires that in all averments of fraud or mistake, the circumstances constituting fraud or mistake shall be stated with particularity.

Rule 9(f) of the Federal Rules of Civil Procedure, provides that for the purpose of testing the sufficiency of a pleading, averments of time and place are material and shall be considered like all other averments of a material matter.

This Court, in considering motions to dismiss under Rule 7012 for a failure to state a claim upon which relief can be granted, is aware that: (1) the purpose of such a motion is to test the legal sufficiency of a complaint; (2) the court should view the complaint in a light that accepts the truth of all material factual allegations and draw all reasonable inferences in favor of the plaintiff; (3) the complaint need only meet the liberal requirement of a short and plain statement of the claim that will give the defendant fair notice of what the plaintiff's claim is and the grounds upon which it rests; and (4) nevertheless, the complaint should be well pleaded and it must contain more than mere conclusory statements that a plaintiff has a valid claim of some type and is thus deserving of relief, See In re Johns Insulation, Inc., 221 B.R. 683, 687 (Bankr. E.D.N.Y. 1998) and the cases cited therein.

The Court is also aware that: (1) a motion to dismiss pursuant to Rule 7012 may not be granted unless it appears beyond a doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief; and (2) the Bankruptcy Court is not entitled to consider matters outside the pleadings or to weigh evidence that might be presented at trial. See In Re Albion Disposal, Inc., 217 B.R. 394, 401 (W.D.N.Y. 1997) ("*Albion Disposal*").

The Court is further aware that: (1) justice requires that the defendant be served with a complaint which states the particular statute or code section relied upon by the plaintiff and a set of facts to provide the defendant with enough information to formulate and file an answer, See In re Marceca, 127 B.R. 328, 332 (Bankr. S.D.N.Y. 1991); (2) if the plaintiff is predicated his cause of action upon fraud, he must do so with specificity as required by Rule 9(b) of the Federal Rules of Civil Procedure, See Marceca at 332-33; and (3) if the Court relies upon matters found outside the complaint, it is required to convert the motion to dismiss into a motion for summary judgment, See Johns Insulation, Inc. at 685.

In addition, The Court is aware that, just as debtors generally will not oppose a motion for an extension of the Bar Date when they know that the creditor or the trustee can establish cause and has a potentially valid cause of action under Section 523(a) or Section 727(a), debtors generally will not file a motion to dismiss a complaint in an adversary proceeding brought under Section 523(a) or Section 727(a) when they believe that the complaint was simply inartfully prepared. This is because debtors know that courts, in the interests of justice and as they attempt to balance the policies of affording a debtor a fresh start as soon as possible with the direction that certain debts not be discharged and that less than honest or uncooperative debtors not receive a discharge, are reluctant to dismiss an adversary proceeding brought under Section 523(a) or Section 727(a) simply because of an inartfully drawn pleading where facts and circumstances exist that might entitle the Plaintiff to relief.

**B. The Complaint in this Case and the Causes of Action Against Marjorie Hart and against John Hart under Sections 523(a)(2)(A) and 523(a)(4)**

The Complaint in this Adversary Proceeding: (1) simply paraphrased or parroted the statutory provisions of Sections 523(a)(2)(A), 523(a)(4) and 727(a)(2)(A), (3), (4)(A) and (5); (2) did not set forth any specific facts to support a cause of action under any of the stated Sections and to demonstrate that the Plaintiffs were entitled to relief; (3) did not to give the Debtors any notice of the underlying grounds for the Plaintiffs' legal conclusions so that they could defend against them; (4) failed to set forth with specificity, as required by Rule 9(b) of the Federal Rules of Civil Procedure, facts and circumstances giving rise to the Plaintiffs' allegations of fraud under Sections 523(a)(2)(A) and 523(a)(4); and (5) failed to demonstrate that Marjorie Hart owed any debt to the Plaintiffs that could be determined to be nondischargeable under Section 523(a).

In addition, even after the Court, in the interests of justice and contrary to the directions of the Court in *Albion Disposal*, afforded the Plaintiffs an additional opportunity to present specific and relevant facts, the Answering Affidavit and the Attorney Affidavit still failed to set forth any facts that would support a cause of action against John Hart under Section 523(a)(2)(A) or Section 523(a)(4), or against Marjorie Hart under Section 523(a) or 727(a).

For those reasons, the Court dismissed the Complaint in its entirety against Marjorie Hart and the Section 523(a)(2)(A) and 523(a)(4) causes of action against John Hart.

To the extent that the Plaintiffs might now assert that they should be allowed to amend the Complaint to assert that the debts due to them from John Hart should be determined to be nondischargeable pursuant to Section 523(a)(6) for willful and malicious injury, because he converted some or all of the assets of RCSA, Inc. to his own use and benefit, Plaintiffs failed to set forth in the Complaint or in the Answering Affidavit: (1) a specific allegation that the provisions of Section 523(a)(6) were applicable; (2) sufficient facts to demonstrate that they were entitled to relief

under Section 523(a)(6); or (3) sufficient facts to put John Hart on notice that they were alleging a potential cause of action for willful and malicious injury under Section 523(a)(6). Therefore, since the Bar Date has passed, and it would not be in the interests of justice to allow an amendment to the Complaint to include a Section 523(a)(6) cause of action, any such cause of action is now unavailable to the Plaintiffs.

**C. The Complaint in this Case and the Causes of Action Against John Hart under Section 727(a)**

Not every pre-petition or post-petition act or omission by a debtor which might lead one to conclude that the debtor was less than completely honest and cooperative will result in the denial of a discharge under Section 727(a). It is only those specific acts and omissions provided for by Congress in Section 727(a) that can result in a denial of discharge, and for that purpose, the statute should be strictly construed.

After reviewing all of the Plaintiffs' submissions, it appears that the remaining assertions the Court must consider under Section 727(a) are that the discharge of the Debtor, John Hart, should be denied because: (1) John Hart may have converted some of the raw materials and unfinished inventory of RCSA, Inc. to his own use and benefit; (2) if John Hart did convert some of the raw materials or unfinished inventory of RCSA, Inc. to his own use and benefit, and some of those assets were still in existence and under his possession and control at the time he filed his petition, he had failed to schedule them or advise the Trustee of their existence; and (3) John Hart had failed to schedule his interest in Adteck Marketing at the time he filed his original schedules and statements.

These allegations, even if true, would not result in a denial of the discharge of John Hart under Sections 727(a)(2)(A), 727(a)(3), 727(a)(4)(A) or 727(a)(5).

**1. Section 727(a)(2)**

In their Complaint, the Plaintiffs alleged that the Debtors, with the intent to hinder, delay and defraud the Plaintiffs, upon information and belief, had transferred, removed, destroyed, mutilated or concealed, or had permitted to be transferred or removed, destroyed, mutilated or concealed, property of the Debtors within one year prior to the filing of their bankruptcy.

Section 727(a)(2)<sup>6</sup>, as relevant to the Plaintiff's Complaint, addresses a transfer or concealment of property of the debtor with the intent to hinder, delay or defraud a creditor. The only factual allegations that the Plaintiffs have made which are relevant to a cause of action under Section 727(a)(2)(A) are that the Debtor, John Hart, may have disposed of or concealed property of RCSA, Inc. in which the Plaintiffs had a security interest with the intent to hinder, delay or defraud them. These factual allegations, which were not contained in either the Complaint or the Answering Affidavit but were first set forth in the Attorney Affidavit, even if true, would not meet the requirements of Section 727(a)(2)(A) because: (1) the property in question was the property of RCSA, Inc., not the property of the Debtor, John Hart, See *In re Colodner*, 147, B.R. 90, 93 (Bankr. E.D.N.Y. 1992) and the cases cited therein ("Although the debtor may have a derivative interest in his corporation's assets, the term "property of the debtor"... has reference to property in which the debtor has a direct proprietary interest"); (2) the undisputed evidence presented to the Court indicates

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<sup>6</sup> Section 727(a)(2) provides that:

(a) The court shall grant the debtor a discharge, unless-

(2) the debtor, with intent to hinder, delay, or defraud a creditor or an officer of the estate charged with custody of property under this title, has transferred, removed, destroyed, mutilated, or concealed, or has permitted to be, transferred, removed, destroyed, mutilated, or concealed-

(A) property of the debtor, within one year before the date of

11 U.S.C. §727(a)(2) (1999).

that RCSA, Inc. was insolvent in September and October 1997, so that John Hart, even though he was the majority shareholder, had no equity in the assets of RCSA, Inc.; (3) there is no evidence that John Hart, who alleged that he only cooperated with PEM in its obtaining the inventory and raw materials of RCSA, Inc. in which it asserted an interest, transferred or concealed any of those assets of RCSA, Inc. with an intent to hinder, delay or defraud the Plaintiffs.

**2. Section 727(a)(3)**

In their Complaint, the Plaintiffs also alleged that the Debtors had concealed, destroyed, mutilated, falsified or failed to keep or preserve any recorded information from which their financial condition or business transactions might be ascertained. However, neither the Complaint, Answering Affidavit, Attorney Affidavit, or other submissions on behalf of the Plaintiffs identify any specific records relevant to John Hart's personal financial condition or his business transactions, either in general or in connection with RCSA, Inc., which he has concealed, destroyed, mutilated, falsified or failed to keep or preserve. Furthermore, the Plaintiffs have not indicated how the failure to keep any particular books and records, including any specific book or records of RCSA, Inc.<sup>7</sup>, would be necessary or material in his bankruptcy case for the interested parties to properly understand John Hart's financial condition or his business transactions which have not otherwise been explained. This is what is required by Section 727(a)(3).<sup>8</sup> See, In re Trogdon, 111 B.R. 655, 658 (Bankr.

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<sup>7</sup> In some cases the books of a corporation or a partnership may be material to a proper understanding of the debtor's financial condition, if not otherwise explained. See: *Matter of Esposito*, 44 B.R. 817 (Bankr. S.D.N.Y. 1984) ("*Esposito*").

<sup>8</sup> Section 727(a)(3) provides that:

(a) The court shall grant the debtor a discharge, unless—

(3) the debtor has concealed, destroyed, mutilated, falsified, or failed to keep or preserve any recorded information, including books, documents, records, and papers, from which the debtor's financial

N.D.Ohio 1990) and *Esposito* (the purpose of this provision is to ensure that the trustee and creditors receive sufficient information to trace a debtor's financial history for a reasonable period past to present).

**3. Section 727(a)(4)(A)**

In their Complaint, the Plaintiffs further alleged that the Debtors had knowingly and fraudulently made false accounts at their 341 Meeting. However, the Complaint did not set forth any specific false oaths or accounts that the Debtors had made which would be grounds for the denial of John Hart's discharge under Section 727(a)(4)(A)<sup>9</sup>. In the Answering Affidavit, the attorney for the Plaintiffs alleged that: (1) at the 341 Meeting of Creditors, Hart had denied that he removed any assets of RCSA, Inc. from the Geneva location for his own benefit and that he used any such assets for a business conducted by Adteck Marketing; and (2) he failed to schedule a bank account with the Bank of Ireland.

John Hart denied the allegations that he ever had or failed to schedule a bank account at the Bank of Ireland and he explained the basis for what may have been the Plaintiffs' confusion

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condition or business transactions might be ascertained, unless such act or failure to act was justified under all of the circumstances of the case[.]

11 U.S.C. §727(a)(3) (1999).

<sup>9</sup> Section 727(a)(4)(A) provides that:  
(a) The court shall grant the debtor a discharge, unless—

(4) the debtor knowingly and fraudulently, in or in connection with the case—

(A) made a false oath or account[.]

11 U.S.C. §727(a)(4)(A) (1999).

regarding his possible ownership of such an account. Thereafter, neither the Trustee nor the Plaintiffs pursued this allegation.

John Hart also denied the allegations regarding the assets of RCSA, Inc., both at the Section 341 Meetings and in connection with the Adversary Proceeding, and he provided the Mari Affidavit which supports his denials and contradicts the Plaintiffs' allegations. John Hart's version of these matters, which involved the assets of RCSA, Inc., a non-operational, insolvent corporation, of which John Hart was the majority shareholder, was fully disclosed, and nothing in the Plaintiffs' submissions, including the Buksar Affidavit, raises a material issue of fact as to whether John Hart's version of the matter was fraudulently made.<sup>10</sup>

Furthermore, if John Hart was in possession of any of the assets of RCSA, Inc. when he filed his petition, those assets would belong to RCSA, Inc. and would not be administered by the Trustee and, therefore, would not be material assets of his estate which were not disclosed.

The only other allegation made by the Plaintiffs with regard to a potential cause of action under Section 727(a)(4) is that the Debtor, John Hart, failed to schedule his Adteck Marketing d/b/a in his original schedules. Although this appears to be true, it also appears that the Debtor did intend to file amended schedules very early in the case, and, in fact, the amended schedules filed on October 16, 1998 were signed by the Debtor's new attorney on October 5, 1998, a date even before the initial Section 341 Meeting was conducted on October 16, 1998. In view of the facts that: (1) the Debtor, John Hart, very early in the case after a change of attorney, amended his schedules to include the Adteck Marketing d/b/a; (2) Adteck Marketing was not an active d/b/a at the time of the filing; (3) the Adteck Marketing d/b/a was discussed at the October 16, 1998 Section 341 Meeting; (4) the

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<sup>10</sup> See unpublished decision in *In Re Pierrri* (Case No. 97-20461, dated 4/21/98) for the elements necessary to prove a cause of action under Section 727(a)(4).



Trustee has not pursued a Section 727(a)(4) cause of action; and (5) there is not evidence that John Hart fraudulently failed to schedule the asset, any failure to initially schedule this d/b/a, which does not appear to have been a material asset at the time of the filing of the petition, would not warrant the denial of a discharge under Section 727(a)(4).

**4. Section 727(a)(5)**

In their Complaint, the Plaintiffs also alleged that the Debtors were unable to satisfactorily explain a loss of assets utilized in the operation of RCSA, Inc. To the extent that Hart may have failed to satisfactorily explain any loss of the assets of RCSA, Inc., an insolvent, non-operational corporation of which he was the majority shareholder, which he had asserted that he has fully explained, the Plaintiffs have failed to demonstrate how such an unexplained loss, if there was one, would have been a loss or deficiency of assets to meet John Hart's liabilities. This is what is required by Section 727(a)(5)<sup>11</sup>. See *In re Chachra*, 138 B.R. 397, 403 (Bankr. S.D.N.Y. 1992).

**5. Summary**

Given that: (1) the Complaint completely failed to set forth any specific facts, as required by Rule 8 of the Federal Rules of Civil Procedure; (2) even if the Court considers all of the factual information alleged in the additional submissions and arguments made on behalf of the Plaintiffs, and treats the Dismissal Motion as one for a Motion for Summary Judgment, the Plaintiffs have

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<sup>11</sup> Section 727(a)(5) provides that:

(a) The court shall grant the debtor a discharge, unless—

(5) the debtor has failed to explain satisfactorily, before determination of denial of discharge under this paragraph, any loss of assets or deficiency of assets to meet the debtor's liabilities[.]

<sup>11</sup> U.S.C. §727(a)(5) (1999).

failed to establish any disputed material facts or that the Debtor, John Hart, had committed any of the acts or omissions set forth in Sections 727(a)(2)(A), (3), (4)(A) or (5) which would warrant the Court denying him a discharge; and (3) nothing in the Plaintiff's Complaint or in their submissions has demonstrated that there are sufficient grounds, which, in the interests of justice, would warrant the Plaintiffs being afforded the opportunity to amend their Complaint in the Adversary Proceeding, the Plaintiffs' causes of action under Section 727(a) must be dismissed.

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**CONCLUSION**

The Dismissal Motion as it relates to any cause of action alleged by the Plaintiffs under Section 727(a) is in all respects granted, and the Plaintiffs request to amend their Complaint is in all respects denied.

If, within thirty (30) days of the entry of the Decision & Order, the parties have not advised the Court that they have settled upon a reasonable attorney fee to be paid by the Plaintiffs to Marjorie Hart, the Court will set a hearing to determine such a reasonable attorney fee.

**IT IS SO ORDERED.**

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/s/  
**HON. JOHN C. NINFO, II**  
**U.S. BANKRUPTCY JUDGE**

**Dated: May 4, 1999**