THIS OPINION IS NOT INTENDED FOR PUBLICATION

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF OHIO
EASTERN DIVISION

In re:	)	Chapter 7
	)	
MICHAEL F. PALUMBO,	)	Case No. 97-50431
CHRISTINE M. PALUMBO,	)	Adv. No. 97-5153
Debtors.	)	
	)	JUDGE MARILYN SHEA-STONUM
Cadlerock Joint Venture, L.P. and	)	
The Cadle Company II, Inc.,	)	
Plaintiffs,	)	
	)	**OPINION DENYING OBJECTION TO**
v.	)	**DISCHARGE BASED ON 11 U.S.C.**
	)	**§ 727(a)(4)**
Michael F. Palumbo, et al.,	)	
Defendants.	)	

This matter is before the Court on Plaintiffs' Complaint (Objection to Discharge) and Defendants' Answer. This matter is a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(J). This Court has jurisdiction over this matter pursuant to 28 U.S.C. § 157(a) and (b)(1) and by the Standing Order of Reference entered in this District on July 16, 1984.

I. FACTS

A. The Bankruptcy Filing

On February 21, 1997 (the "Petition Date"), Defendants filed a chapter 11 petition as Michael and Christine Palumbo *dba* Mack Properties. In their Schedules of Assets and

Liabilities, filed on March 5, 1997, Defendants listed total assets valued at approximately $3,357,215 and total liabilities estimated at approximately $6,356,761.

Before the Petition Date, Defendants rented various properties; Defendants' income consisted primarily of rent checks from their tenants. [Exhibit 63 (Schedule I)]. Defendants deposited rental income into a business checking account at Ravenna Savings entitled "Mack Properties".

B. Defendants' Use of Angela Palumbo's Bank Account

On February 10, 1986, Angela Palumbo, Defendants' oldest of four children [Exhibit 63 (Schedule I)], opened a personal checking account which she maintained at First National Bank of Ohio, Account #1610-7747 (the "FNB Account"). Defendants were not listed as owners of the FNB Account. [Exhibit10].

In or about July 1996, a creditor of Defendants swept approximately $15,000 to $20,000 of rental income which Defendants had deposited into the Mack Properties bank account. In order to protect their rental income from garnishment and to pay household bills and expenses, Defendants stopped using the Mack Properties bank account and started depositing rent checks into the FNB Account. [Exhibit A/S-7, pp. 33-34]. Defendants' use of the FNB Account can be summarized as follows:

a. Between February 10, 1996 and July 23, 1996, the FNB Account balance did not exceed $70.00.

b. Between July 23, 1996 and September 24, 1996, approximately $6,755.00 was deposited into the FNB Account, and checks totaling $6,673.33 were written out of the FNB Account.

c. On February 18, 1997, $5,326.49, derived in large part from Mack Properties' rental checks, was deposited into the FNB Account. On February 19, 1997, two checks in the total amount of $4,000.00 were written out of the FNB Account. On the Petition Date, a balance of $1,256.74 remained in the FNB Account.

[Exhibits 11-23; Exhibit 26].

Defendants did not list the FNB Account in their Schedules; instead, Defendants listed "none" as to their interest in checking, savings or other financial accounts. Mr. Palumbo testified at trial that he believed that the funds derived from rental payments which Defendants had deposited into the FNB Account had been exhausted prepetition. After the Petition Date, Defendants did not deposit any rental income into the FNB Account but instead deposited such income into a debtor in possession bank account opened by Defendants on March 1, 1997 .[1] [Exhibits 55-71].

On April 11, 1997, at Defendants' section 341(a) meeting of creditors, Defendant Michael Palumbo disclosed that Defendants used the FNB Account prepetition for a period of several months. Mr. Palumbo explained that Defendants could no longer deposit rental checks into the Mack Properties bank account because of the threat of garnishment. [Exhibit A/S-7, pp. 31-36]. Mr. Palumbo stated at the 341(a) meeting that "we paid people with third-party checks, and we deposited some of the checks into my daughter's checking account to pay the bills to survive." [Exhibit A/S-7, p. 33]. Defendants informed the representative of the U.S. Trustee that Defendants would provide him with the account statements for the FNB Account [Exhibit A/S-7, pp. 35-36].

On September 8, 1997, Plaintiffs filed this adversary proceeding alleging that

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[1] Postpetition, Defendants did make limited deposits into the FNB Account, and based on entries in the check register, some family expenses appear to have been paid out of the FNB Account. [Exhibit 26]. On May 10, 1997, a money order in the amount of $120.00, payable to Mike Palumbo, was deposited into the FNB Account [Exhibit A/S-5]. On May 16, 1997, two checks from KELT Revenue, payable to Michael Palumbo, in the amount of $29.33 and $35.65, were deposited into the FNB Account. [Exhibit A/S-6].

Defendants have violated 11 U.S.C. § 727(a)(4)(A) and thus should be denied their discharge. Specifically, Plaintiffs state that Defendants made a false oath by answering "none" to the category requesting Defendants to list all checking, savings or other financial accounts and failing to list the FNB Account in response to that request.[2]

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[2] In the Complaint, Plaintiffs also alleged that Defendants made a false oath by failing to disclose in their Schedules additional bank accounts held in the names of Defendants' children and a bank account held in the name of James Boal. As to the additional bank accounts held in the names of Defendants' children, on July 23, 1998, this Court granted partial summary judgment holding that Defendants did not have an interest in those accounts which would require that Defendants identify those accounts in their Schedules.

Regarding the bank account of James Boal, in the Proposed Findings of Fact and Conclusions of Law which Plaintiffs filed for this proceeding on October 15, 1998, Plaintiffs do not discuss this allegation and appear to have withdrawn the objection to Defendants' discharge based on the omission of this bank account from Defendants' Schedules. Even if Plaintiffs did not withdraw this basis of their objection, Mr. Boal testified at trial that the rental checks provided to him by Defendants and deposited by Mr. Boal into this bank account were in payment of wages owed to Mr. Boal for maintaining Defendants' rental properties, and Plaintiffs provided no evidence to the contrary. Thus, Plaintiffs have not met their burden of proving that Defendants should be denied a discharge based on Defendants' omission of this bank account from their Schedules.

II. LEGAL AUTHORITIES AND ANALYSIS

Section 727(a)(4) provides that "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). The provisions denying a discharge to a debtor are generally construed liberally in favor of the debtor and strictly against the creditor. In re Shoup, 214 B.R. 166, 172 (Bankr. N.D. Ohio 1997).

Pursuant to Fed. R. Bankr. P. 4005, Plaintiffs have the burden of proof in objecting to Defendants' discharge. Plaintiffs must satisfy that burden of proof by the preponderance of the evidence. Adams v. Barclays/American Business Credit (In re Adams), 31 F.3d 389, 393-94 (6th Cir. 1994)(holding that "exceptions to dischargeability under Section 727 . . . require proof by the preponderance of the evidence"); Buck v. Buck (In re Buck), 166 B.R. 106, 109 (Bankr. M.D. Tenn. 1993)(holding that plaintiff failed to show by a preponderance of evidence that errors and omissions from debtor's schedules were knowingly and fraudulently made by debtor or constituted a reckless disregard for the truth).

In determining whether a discharge should be denied in accordance with 11 U.S.C. § 727(a)(4), courts are to evaluate whether (1) the debtor made a statement under oath; (2) the statement was false; (3) the debtor knew the statement was false; (4) the debtor made the statement with fraudulent intent or with reckless disregard for the truth; and (5) the statement related materially to the bankruptcy case. Beaubouef v. Beaubouef (In re Beaubouef), 966 F.2d 174, 178 (5th Cir. 1992). A false oath is material if it "bears a relationship to the bankrupt's business transactions or estate, or concerns the discovery of assets, business dealings, or the existence and disposition of his property." L.B. Cleveland, Inc. v. Bluestone (In re Bluestone), 102 B.R. 103, 108 (Bankr. N.D. Ohio

1989). See also Chalik v. Moorefield (In re Chalik), 748 F.2d 616, 618 (11th Cir. 1984). A false statement or omission in a debtor's schedules can be sufficient to justify the denial of the debtor's discharge pursuant to 11 U.S.C. § 727(a)(4)(A). See Beaubouef, 966 F.2d at 178; Kalvin v. Clawson (In re Clawson), 119 B.R. 851, 852 (Bankr. M.D. Fla. 1990).

The Court may infer a debtor's intent to defraud from the facts and circumstances presented. See Job v. Calder (In re Calder), 907 F.2d 953, 956 (10th Cir. 1990)(affirming decision of bankruptcy court that debtor who practiced as bankruptcy attorney acted fraudulently in omitting from his schedules his ownership interest in mineral rights, two bank accounts and monthly income which was paid to debtor as a partner of a partnership); Fahey Banking Co. v. Parsell (In re Parsell), 172 B.R. 226, 231 (Bankr. N.D. Ohio 1994)(denying objection to discharge although debtor omitted certain truck accessories and guns from his schedules and did not disclose prepetition payments made to debtor's mother and father in his schedules). When a debtor has omitted an interest in property from his schedules, but disclosed that interest at his 341(a) meeting of creditors, courts have found that the intent to defraud or reckless disregard for the truth required to deny a discharge based on 11 U.S.C. § 727(a)(4) is absent. For example, in Shoup, the debtors did not disclose the transfer of their one-half interest in a trucking business in their schedules. However, the debtors did reveal the transfer at the creditors' meeting. The debtors contended that the failure to report the transfer on their bankruptcy schedules was the result of a hasty bankruptcy filing initiated as a result of a creditor's execution upon their personal property. Shoup, 214 B.R. at 176. The court denied an objection to discharge pursuant to 11 U.S.C. § 727(a)(4). The court held that the debtors lacked fraudulent intent, noting that the debtors were forthcoming about the transfer at the creditors' meeting. Id., at 177. See also Cogan v. Barney (In re Barney), 86 B.R. 105,

109 (Bankr. N.D. Ohio 1987)(overruling objection to discharge based on 11 U.S.C. § 727(a)(2) and holding that debtors' disclosure at creditors' meeting of attempted fraudulent transfer of property gave rise to rebuttable presumption in favor of discharge).

In light of Defendants' prepetition use of the FNB Account, Defendants should have listed the FNB Account in their Schedules. Their failure to do so constitutes a false statement under oath. Moreover, the omission relates materially to Defendants' bankruptcy case as it "bears a relationship to the bankrupt's business transactions or estate, or concerns the discovery of assets, business dealings, or the existence and disposition of his property." Bluestone, 102 B.R. at 108.

However, despite the inappropriate omission of the FNB Account from their Schedules, Defendants' disclosure of their prepetition use of the FNB Account at the first creditors' meeting, coupled with their provision of the account statements for the FNB Account to the U.S. Trutee, indicates that Defendants did not omit the FNB Account from their Schedules with fraudulent intent or with reckless disregard for the truth. Having heard Defendant Michael Palumbo's testimony at trial, the Court believes Mr. Palumbo's statement that Defendants did not know that rental income remained in the FNB Account at the time of their bankruptcy filing and did not understand that the FNB Account should have been listed on their Schedules.

As Mr. Palumbo testified, at the time of their bankruptcy filing, Defendants were overwhelmed by foreclosures which were proceeding on many of their rental properties, the related appointment of receivers, attachments of their personal property and garnishments of their income. On the Petition Date, Defendants had more than 50 creditors and liabilities in excess of $6,000,000. [Exhibit 62]. In this situation, it is not surprising that Defendants were not aware of the balance in the FNB Account on the

Petition Date and whether or not that balance, which was less than $1,300, consisted of Defendants' rental income.

Because Defendants disclosed their prepetition use of the FNB Account at the first creditors' meeting, creditors attending that meeting and the U.S. Trustee received notice of the FNB Account. Defendants' provision of this information in this manner negates the inference that Defendants' omission of the FNB Account from their Schedules was done with fraudulent intent.[3]

Given that this Court had found that Defendants lacked fraudulent intent and did not act with reckless disregard for the truth when Defendants omitted the FNB Account from their Schedules, the Court overrules the objection to Defendants' discharge based on 11 U.S.C. § 727(a)(4).

IT IS SO ORDERED.

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MARILYN SHEA-STONUM
Bankruptcy Judge

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[3] Relying on a debtor's voluntary disclosure of assets at the first creditors' meeting to demonstrate an absence of fraudulent intent under § 727(a)(4) encourages debtors to remedy nondisclosure after the filing of their schedules. As discussed by the court in Barney:

> Filing is often done in haste, without time for "reflection" or in depth "advice of counsel". In the bankruptcy process, the first meeting of creditors is, in many ways, the moment of "truth" for the debtors. It is the opportunity for full disclosure. It appears that the incentive for the debtor to disclose all transfers, or attempted transfers, should continue beyond the filing of the petition. . . . No purpose is served in giving debtors a strong incentive to "stonewall" creditors . . . .

Barney, 86 B.R. at 110, *quoting* In re Adeeb, 787 F.2d 1339 (9th Cir. 1986).

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DATED: 7/23/98